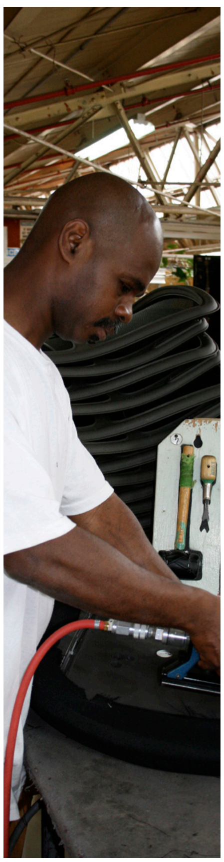
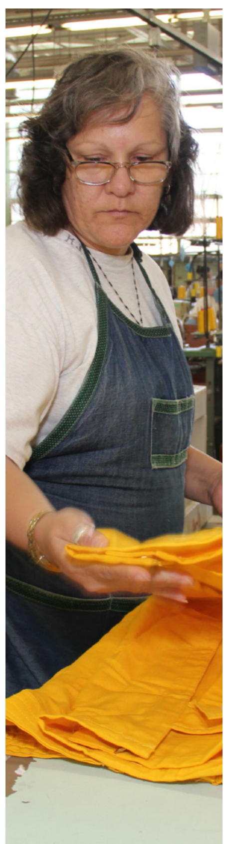
QUALITY PRODUCTS · CHANGED LIVES · A SAFER CALIFORNIA

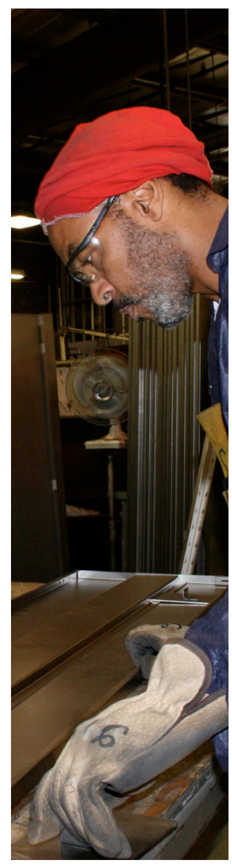
California Prison Industry Authority

Report to the Legislature

FISCAL YEAR 2011-2012







CALPIA

Quality Products ★ Changed Lives ★ A Safer California

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Governor
State of California

California Prison Industry Board

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The Prison Industry Board (PIB) Fiscal Year 2011-12 Report to the Legislature regarding the California Prison Industry Authority (CALPIA) is submitted pursuant to Chapter 1549, Statutes of 1982, as embodied in paragraph 2808 (k) of the California Penal Code which requires the PIB to report to the Legislature in writing on or before February 1, of each year regarding the following:

1. The financial activity and condition of each enterprise under its jurisdiction.
2. The plans of the board regarding any significant changes in existing operations.
3. The plans of the board regarding the development of new enterprises.
4. A breakdown, by institution, of the number of prisoners at each institution, working in enterprises under the jurisdiction of the CALPIA.

Committed to California's Public Safety

The Prison Industry Board

Pursuant to Chapter 1549, statutes of 1982, the Prison Industry Board (PIB) was established in 1983 to oversee California Prison Industry Authority (CALPIA) operations, much like a corporate board of directors. The PIB sets general policy for CALPIA, oversees the performance of existing CALPIA industries, determines which new industries shall be established, and appoints and monitors the performance of CALPIA's CEO/General Manager. The PIB also serves as a public hearing body, charged both with ensuring that CALPIA enterprises are self-sufficient and that they do not have a substantial adverse effect upon the private sector. The PIB actively solicits public input for the decisions it makes to expand existing or develop new prison industries.

The Penal Code[1] Established the California Prison Industry Authority (CALPIA) to:

- Develop and operate manufacturing, agricultural, and service enterprises that provide work opportunities for offenders under the jurisdiction of the California Department of Corrections and Rehabilitation (CDCR), and serve government agencies with products and services commensurate with their needs.

- Create and maintain working conditions within enterprises as much like those which prevail in private industry as possible, to assure offenders assigned therein the opportunity to work productively to earn funds, and to acquire or improve effective work habits or occupational skills.

- Operate work programs for offenders that are self-supporting through the generation of sufficient funds from the sale of products and services to pay all its expenses, thereby avoiding the cost of alternative inmate programming by CDCR. CALPIA receives no annual appropriation from the Legislature.

1. Penal Code Section 2800-2018

CALPIA Mission Statement

The mission of CALPIA is to support the CDCR public safety mission.

CALPIA Program Goal

CALPIA's program goal is to produce trained offenders that have a job skill, good work habits, basic education, and job support in the community when they parole so they never return to prison. CALPIA offenders receive industry accredited certifications that employers require. CALPIA offender programming reduces prison violence and makes communities safer by lowering the frequency of repeat criminal behavior.

Does CALPIA Work?

Over a three year period, beginning in Fiscal Year (FY) 2007-08, CALPIA participants returned to prison, on average, 26 to 38 percent less often than offenders released from the CDCR general population, saving the General Fund millions in incarceration cost avoidance. Additionally, offenders who participate in CALPIA's Career Technical Education (CTE) program are 82 percent less likely to return to prison.

Does CALPIA Save the State Money?

CALPIA's offender programming saves the State General Fund millions annually through lower recidivism, and saves CDCR millions more by providing rehabilitation programs that CDCR does not have to fund.

To achieve its mission, CALPIA has established five main strategic and business goals:

- Achieve Self-Sufficiency
- Build Offender Success
- Exceed Customer Expectations
- Ensure an effective and well-trained workforce
- Promote and Support CALPIA

Correctional Industries

CALPIA manages 57 manufacturing, service, and consumable factories in 24 CDCR institutions. CALPIA provides employment and programming for approximately 7,000 offenders assigned to 5,399 positions annually in manufacturing, consumables, service enterprises, and selling and administration. Administrative offices are located in Folsom, California.

The goods and services produced by CALPIA's enterprises are sold predominately to departments of the State of California, as well as other government entities. CDCR is CALPIA's largest customer, and accounted for 57 percent of all sales in FY 2011-12, down from 62 percent in FY 2010-11. Other major State customers include The Department of Motor Vehicles, the Department of State Hospitals, the Department of Health Care Services, the Department of Transportation (CalTrans), the Department of Developmental Services (DDS), the Department of General Services (DGS), the Department of Forestry and Fire Protection (CAL FIRE), the California National Guard, and the California Highway Patrol (CHP).

All CALPIA offender participants must achieve a General Education Development (GED) degree within two years to continue participating in CALPIA.

Joint and Free Venture Programs

On behalf of CDCR CALPIA manages California's Joint Venture Program (JVP), which is responsible for implementing the Prison Inmate Labor Initiative, Proposition 139 of 1990. Under its provisions, private businesses may set up business operations inside California correctional facilities and hire offenders. This includes only those businesses that are starting a new company, expanding an existing business, or relocating to California.

CALPIA also manages the Free Venture Program (FVP), which operates in much the same way as the JVP, except it is located within California's juvenile facilities.

This unique relationship is a cooperative effort of private industry and the State of California, benefitting businesses, victims, and the state, while preparing offenders for successful reintegration into the community.

Offenders are paid a comparable wage that is then subject to deductions for room and board, crime victim compensation, prisoner family support, government ordered restitution (child support), and mandatory offender savings for release. In addition, offender-employees pay federal and state taxes. The JVP disbursed more than $100,000 for crime victim restitution in FY 2011-12. As of October 2012, local government correctional facilities may also participate in the JVP.

Inmate Employability Program

CALPIA developed the Inmate Employability Program (IEP) to enhance the ability of offender workers to obtain meaningful jobs upon release and successfully transition from prison to the community and the world of work. This effort supports CALPIA's goal to reduce recidivism and contribute to safer communities.

Through the IEP, CALPIA offender workers are continually evaluated for improvement in job skills, education, experience and work habits. The IEP provides offender workers access to nationally accredited certifications and internal skill proficiency certificates.

The IEP provides transition to employment services and information. Prior to parole, an appointment at the Department of Motor Vehicles is arranged to provide valid identification. Information and forms are provided for a social security card, birth certificate, child support, and veteran's benefits. The IEP also provides access to the CDCR statewide resource guide.

Career Technical Education

The CALPIA Career Technical Education (CTE) program[2], established by CALPIA in 2006 as a pilot, gives offenders an opportunity

2. Under Penal Code Section 2805, CALPIA may initiate and develop new vocational training programs as well as assume jurisdiction over existing vocational training programs

to gain hands-on experience in real world training, as well as work opportunities performing construction and facility maintenance for institutions and communities. To date, the CALPIA CTE program has been the most effective rehabilitation program in California and also provides a well-trained labor force for maintenance and construction projects at reduced cost.

In November, 2012 the Prison Industry Board approved an assessment study of the CALPIA CTE program from FYs 2007-08 through 2010-11. The report documents that cumulatively, CALPIA CTE graduates have a recidivism rate of 7.13 percent, the lowest of any rehabilitative program. Additionally, the recidivism cost avoidance from the CALPIA CTE program is over $10 million during the period. The CALPIA CTE Construction Services and Facilities Maintenance Enterprise has saved state and local governments $2.5 million in project cost avoidance since 2007. The full study is available at www.calpia.ca.gov.

The CALPIA CTE program is the first of its kind in the nation to partner an offender rehabilitation program with trade unions to meet the rehabilitative needs of offenders. CALPIA CTE participants perform various construction activities such as the fabrication of modular buildings and renovations of state-owned assets, including parks and prisons. CTE participants also renovated and re-opened a commercial diving training facility within a state prison and now utilize that facility for vocational education training in commercial diving and welding.

The CALPIA CTE program is divided into five areas:

1. Carpentry
2. Iron working
3. Construction labor
4. Commercial diving
5. Facilities maintenance

Today, because CALPIA is entirely responsible for funding the CTE program, CALPIA has reluctantly reduced enrollment in order to meet its statutory obligation to maintain self-sufficiency. As of October, 2012, enrollment in the CALPIA CTE program is down to 100 participants, from a high of 258 participants in FY 2009-10.

The Prison Industry Board has approved CALPIA fully funding the CTE program through June, 2013. Faced with a reduction in revenues, the ending of program support funds from CDCR, along with increasing obligations for Other Post-Employment Benefits (OPEB) for its civil service employees, it is unlikely CALPIA can continue to self-fund the CALPIA CTE program.

California Identification Project

From September 2010 through 2011, CALPIA partnered with CDCR and the California Department of Motor Vehicles to design, develop, implement and administer the California Identification (CAL ID) project as a one-year pilot program to provide offenders with valid California Identification cards upon parole. More than 8,000 identification cards were distributed to the paroling populations of nine institutions during the period.

In January, 2013, CALPIA will continue managing a smaller ID program available to paroling CALPIA offenders at CALPIA locations and non-CALPIA offenders on a space available basis. CALPIA will also offer the CAL ID program to county jails on a reimbursable basis.

CALPIA Reduces Recidivism, Saves Money and Increases Public and Prison Safety

CALPIA prepares offenders for productive lives and reduces incarceration costs. Paroled offenders who participated in CALPIA programs are less likely to return to prison than general population offenders. Although there may be other relevant factors that contribute to lowering recidivism, CALPIA participants are significantly more likely to become productive citizens that pay taxes instead of costing California taxpayers approximately $45,006 per year.[3]

The recidivism rate of CALPIA participants is an essential measure of the organization's success. Over a three-year period, beginning in FY 2007-08, CALPIA participants returned to prison, on average, 26 to 38 percent less often than offenders released from the CDCR general population, saving the General Fund millions in incarceration cost avoidance. Additionally, offenders who participate in CALPIA's CTE program are 82 percent less likely to return to prison.

CALPIA provides CDCR over 7,000 alternative offender programming positions annually, thereby saving CDCR more than $11 million annually in General Fund costs for rehabilitation positions[4] that CDCR does not have to fund.

CALPIA Reduces Recidivism

Fiscal Year	Total CALPIA Parolees	Total CDCR Parolees	1 Year			2 Years			3 Years		
			CALPIA Percent	CDCR Percent	Variance Percent	CALPIA Percent	CDCR Percent	Variance Percent	CALPIA Percent	CDCR Percent	Variance Percent
10/11*	1,402		20.40%								
09/10*	1,364	105,598	23.61%	45.70%	48.34%	33.65%					
08/09*	1,471	112,934	27.46%	45.20%	39.25%	38.55%	56.90%	32.25%	42.96%		
07/08	1,549	116,063	31.18%	47.50%	34.36%	42.09%	59.20%	28.90%	46.80%	63.70%	26.53%
06/07	1,693	115,254	30.89%	47.90%	35.51%	43.89%	60.50%	27.45%	48.32%	65.10%	25.78%
05/06	1,646	108,662	31.11%	49.10%	36.64%	44.11%	62.50%	29.42%	50.12%	67.50%	25.75%
					Average Variance 38.82%			Average Variance 29.51%			Average Variance 26.02%

* Data was unavailable at the time this report was published

CALPIA Recidivism Data is based on the updated Recidivism Methodology as of August 16, 2012

CDCR data updated based on the 2012 Adult Institutions Outcomes Evaluation Report

3. CDCR, Corrections/Year at a Glance, Fall, 2011

4. Legislative Analyst's Office (2011) Rehabilitation Programs (http://www.lao.ca.gov/laoapp/LAOMenus/Sections/crim_justice/6_cj_inmatecost.aspx?catid=3)

CALPIA Invests in Training and Rehabilitation

CALPIA invests in curricula for offenders, including 18 programs that offer nationally recognized accredited certification such as optometry, dental technology, food handling, automotive service, laundry, commercial baking, agriculture, welding, metal stamping, industrial safety and health, electrical systems, mechanical systems and maintenance. CALPIA offenders may also earn certificates of proficiency in occupational disciplines to validate skills and abilities obtained during their time employed by CALPIA (see accredited certifications, below).

FY 2011-12 Training Highlights

- CALPIA added Workers Occupational Safety and Health (WOSH), and International Organization for Standards (ISO) Internal Quality Auditor training. The 60 offenders that obtained ISO Internal Quality Auditor certification are the first in the nation to do so.
- CALPIA added seven new industrial certification programs from TPC Training Systems, primarily in the areas of metal fabrication, tool and die, and maintenance, for a total of 60 new accredited skill certifications.
- 1,147 CALPIA participants received a certificate of proficiency and 1,127 participants successfully completed an accredited certification program, a 237 percent increase (334) from FY 2010-11. Of those that completed an accredited certification program, 95 were graduates of CALPIA's CTE program.

Accredited Certifications

American Board of Opticianry
Optician

American Institute of Baking
Science of Baking
Foundations
Ingredient Technician
Bread/Rolls
Cake/Sweet Goods

American Welding Society
GMAW-1
GTAW-1
GTAW-2
GTAW-3

Association for Linen Management
Certified Linen Technician
Certified Washroom Technician
Certified Laundry Linen Manager

Automotive Service Excellence
Medium/Heavy Truck: Gasoline Engines
Medium/Heavy Truck: Diesel Engines
Medium/Heavy Truck: Drive Train
Medium/Heavy Truck: Brakes
Medium/Heavy Truck: Suspension/Steering
Medium/Heavy Truck: HVAC
Medium/Heavy Truck: PMI
Special: Exhaust Systems

CA Department of Food & Agriculture
Artificial Insemination License
Pasteurizer License
Sampler/Weigher License

Electronics Technicians Association
Customer Service Specialist
Certified Electronics Technician
Journeyman (Industrial)

Federal Emergency Management Agency
Decision Making
Effective Communication
Hazardous Materials

Library of Congress – Braille
Literary Transcribing
Literary Proofreading
Mathematics Transcribing
Mathematics Proofreading
Music Transcribing

National Institute of Metalworking Skills
Machining, Level I
Metal Forming, Level I
Metal Stamping, Level II

National Restaurant Association
ServSafe Essentials
ServSafe Food Handler

North American Technician Excellence
Installation or Service for:
Air Conditioning
Air Distribution
Heat Pumps
Gas Heat
Oil Heat

Overton–Forklift Operator
Warehouse Pallet Jack/ Forklift
Construction Forklift

Printing Industries of America
Sheetfed Offset Press
Web Offset Press
Bindery
Pre-Press

Productivity Training Corporation
Dental Technician

Stiles Machinery Inc.
Intermediate Weeke Machining

TCP Training System
Type: Fundimentals/Core Competencies
(Series 100)
101 Reading Blueprints
102 Reading Schematics and Symbols
103 Mathematics in the Plant
104 Making Measurements
105 Metals in the Plant
106 Nonmetals in the Plant
107 Hand Tools
108 Portable Power Tools
109.1 Industrial Safety and Health
110 Troubleshooting Skills

TCP Training System (continued)
Type: Electrical Systems
(Series 200)
201 Basic Electricity and Electronics
202 Batteries and DC Circuits
203 Transformers and AC Circuits
204.1 Electrical Measuring Instruments
205.1 Electrical Safety and Protection
206 DC Equipment and Controls
207 Single Phase Motors
208 Three Phase Systems
209 AC Control Equipment
210 Electrical Troubleshooting
211 Electrical Safety – Understanding NFPA 70E

TCP Training System (continued)
Type: Mechanical Systems
(Series 300)
301 Basic Mechanics
302 Lubricants and Lubrication
303.1 Power Transmission Equipment
304 Bearings
305 Pumps
306 Piping Systems
307 Basic Hydraulics
308 Hydraulic Troubleshooting
309 Basic Pneumatics
310 Pneumatic Troubleshooting

TCP Training System (continued)
Type: Mechanical Maintenance Applications
(Series 340)
341 Mechanical Drive Maintenance
342 Mechanical and Fluid Drive Systems
343 Bearing and Shaft Seal Maintenance
344 Pump Installation and Maintenance
345 Maintenance Pipefitting
346 Tubing and Hose System Maintenance
347 Valve Maintenance & Piping Sys. Protection

TCP Training System (continued)
Type: Building and Grounds
(Series 360)
361 Introduction to Carpentry
362 Constructing the Building Shell
363 Finishing the Building Interior
364 Structural Painting
366 Flat Roof Maintenance
367 Plumbing Systems Maintenance
375 Landscaping Maintenance

TCP Training System (continued)
Type: Welding
(Series 420)
416 Blueprint Reading for Welders
417 Welding Principles
418 Oxyfuel Operations
419 Arc Welding Operations

TCP Training System (continued)
Type: Custodial Maintenance
(Series 450)
451 Cleaning Chemicals
452 Floors and Floor Care Equipment
453 Maintaining Floors and Other Surfaces
454 Rest Room Care
455 Carpet and Upholstery Care

Financial Activity of CALPIA

Financial Overview

CALPIA recorded an $8.86 million (M) decrease in net assets in FY 2011-12, compared to a $15.3 M decrease during FY 2010-11. The FY 2012-13 Mid Year Revise (MYR) expects an additional decrease in net assets of $4.1 M. The primary component of the FY 2011-12 decrease in net assets is a $6.26 M charge for depreciation on equipment. An additional factor that contributed to the loss was a substantial increase in raw material prices for sales contracts for products and services 12 months into the future. These increases were not passed on to customers in a timely manner. Alternately, sales of products and services to CDCR reduced considerably as a result of correctional realignment with sales decreasing 7.87 percent, including a complete cancellation of non-food product orders by CDCR in the 4th quarter. Other major factors that contributed to this loss were a $700,000 increased expense for Other Post-Employment Benefits (OPEB), a $300,000 increase in CALPIA's pro-rata payment to the State, and other significant impacts (see Significant Impacts).

Operating Revenues

The FY 2012-13 Mid-Year Revise (MYR) anticipates revenues of $165.1 M, a decrease of 4.4 percent from FY 2011-12 audited revenues of $172.7 M. The MYR anticipates CALPIA utilizing up to 5,399 offender positions, compared to 4,870 positions in FY 2011-12. CALPIA anticipates employing 542 free staff in FY 2012-13, which is a 3.9 percent reduction from the previous year.

In the past five years, CALPIA's revenues have declined 17.5 percent from $209.5 M in FY 2007-08 to $172.7 M in FY 2011-12. The largest product declines since FY 2007-08 are Modular Construction (64 percent decrease), Furniture (58 percent decrease), and Optical (47.8 percent decrease).

CALPIA Balance Sheet

The CALPIA Balance Sheet at June 30, 2012, shows that current assets are five times greater than current liabilities and almost twice the amount of total liabilities. These financial indicators reflect that CALPIA is well positioned to meet its short term and long term obligations.

CALPIA remains optimistic about the future of successful business enterprises, supported by a dedicated and qualified workforce, working in partnership with satisfied customers that create the best opportunities for the rehabilitation of offender workers, resulting in a safer California.

Significant Impacts

AB 109 Public Safety Realignment

Governor Brown signed AB 109 (Chapter 15, 2011), Committee on Budget: Criminal Justice Alignment, which redirected thousands of parolees and new offenders to the jurisdiction of counties, starting in October, 2011. The effects of this re-alignment reduced CDCR's purchases in FY 2011-12, which has led to reductions in CALPIA's offender workforce. AB 109 will continue to impact CALPIA revenues by an estimated $5.5 M in FY 2012-13 due to the planned 12 percent reduction in the offender population. This will further reduce opportunities to employ offenders. CALPIA estimates that as a result of the revenue reduction from realignment, a total of up to 725 offender positions, and up to 72 civil service positions will be eliminated before the full impact of AB 109 is realized.

Reduced Reimbursements for Career Technical Education

In 2008, CALPIA entered into a three-year contract with CDCR to manage the Career Technical Education (CTE) program for $3.08M per year. The CTE program has recorded the lowest recidivism rate of any offender rehabilitation program with a cumulative recidivism rate of 7.13 percent. After the second year, the funding level from CDCR was halved to

$1.54 M. In FY 2010-11, CDCR provided $800,000 and then ceased providing reimbursements to CALPIA. In FY 2011-12, CALPIA self-funded a reduced CALPIA CTE program. The FY 2012-13 Mid Year Revise provides funding of $1.2M from CALPIA with no reimbursement from CDCR for this highly successful program.

Postemployment Benefits Other than Pensions

Under Governmental Accounting Standards Board (GASB) Statement No. 45 (GASB 45)—Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions, the State is required to recognize the cost of retiree health benefit programs on an accrual basis rather than on a pay as you go basis. The State Controller informed CALPIA that its share of the State's net unfunded OPEB obligation is $7.0 M for FY 2011-12, up from $6.3 M in FY 2010-11. CALPIA recorded these amounts as a "selling and administrative" expense on the operating statement in addition to the actual payments made for OPEB. The State does not maintain a separate pool of assets to finance future retiree healthcare benefits. As one of the few state agencies required to fund the OPEB obligation from its own proprietary fund, CALPIA actively monitors the costs of retiree health benefits in accordance with Generally Accepted Accounting Principles and the funding policies of the State.

As of June 30, 2012, the CALPIA balance sheet reflects a net OPEB obligation of $32.3 M. CALPIA funds these obligations by setting aside cash reserves. In 2013, CALPIA will seek authority to reinvest these set aside funds to minimize future obligations through higher interest earnings.

Court-Mandated Employee Furlough Settlement

Between February 2009 and October 2010, the Governor ordered state workers to take 55 furlough days without pay in an effort to reduce the State's General Fund expenditures. Three court cases challenged the legality of the furloughs. CALPIA accrued $8.6 M in FY 2010-11, anticipating a court order to compensate its employees back pay, including interest, for furlough time imposed upon employees

In January, 2012 an agreement was reached between the Service Employees International Union (SEIU), Local 1000 and the California Attorneys, Administrative Law Judges and Hearing Officers in State Employment (CASE) and the Governor which settled the civil actions filed by those unions.

The total cost of the settlement to CALPIA in FYs 2010-11/12, including additional retirement contributions, was $7.68 M. A reserve of $126,866 remains in anticipation that a final judgment is issued, or a settlement is reached between the Governor and the remaining unions.

Pro Rata Payments to the State

Despite the fact that CALPIA receives no Budget Act appropriation, CALPIA must pay the State its *pro rata* share of costs of State services (Legislature, Department of Finance, Controller, Treasurer, etc.). In FY 2010-11, CALPIA's *pro rata* bill from the State of California was $3.5 M. The FY 2011-12 *pro rata* payment is $3.8 M and will increase to $4.8 M in FY 2012-13.

Application of State Sales Tax

Per the Board of Equalization, unlike any other manufacturer, CALPIA must pay sales tax on purchases of raw materials instead of collecting sales taxes from the end user. Since CALPIA incurs the cost of paying sales tax on materials purchased, those costs must be reflected in the base prices of CALPIA goods and services. CALPIA paid over $3.9 M in Sales and Use Tax to its vendors in FY 2011-12.

Cash as Designated Liabilities

CALPIA maintains cash levels to meet liabilities such as CALPIA's full OPEB obligation, accrued employee vacation, and workers compensation liabilities. CALPIA will seek authority to reinvest this cash to achieve yields that would lessen these liabilities. In addition, Government Code Section 16310(a) authorizes the State Treasurer to transfer idle cash from other funds (not to exceed 10 percent of the fund) to meet the cash needs of the State. CALPIA is not reimbursed for lost interest when this occurs.

Future Impacts

July 1, 2013 Employee Pay Restoration

To assist in achieving budget savings in FY 2012-13, excluded, non-statutory exempt as well as SEIU, and International Union of Operating Engineers (IUOE) employees were subject to the mandatory Personal Leave Program and a 4.62 percent reduction in pay from July 1, 2012 through June 30, 2013. All employees that were included in the PLP will automatically receive a 4.62 percent pay restoration effective July 1, 2013. The financial impact to CALPIA of the pay restoration will be $1.9 M in FY 2013-14.

Scheduled Pay Increase

Employee pay negotiations are conducted by the California Department of Human Resources (CalHR) and are outside the control of CALPIA. Excluded, non-statutory exempt employees and SEIU members are scheduled to receive an Adjusted Pay Range, 3 percent increase to the maximum step of the salary range in each classification, effective July 1, 2013. The impact to CALPIA is estimated to be $1.2 M in FY 2013-14.

Optical Program - Increasing Orders

In FY 2011-12 CALPIA experienced a $0.7 M increase in optical revenue due to increased Medi-Cal participation. Over the last four years, optical sales have decreased 47 percent from $20.98 M in FY 2008-09 to $10.96 M in FY 2011-12. During this period adults between the ages of 18-65 were excluded from the Medi-Cal optical benefit. Under full implementation of the movement of the Healthy Families Program to Medi-Cal in 2013, demand will increase by an estimated 8,000 optical orders each month. This is expected to generate $172,000 per month for those months of full implementation in FY 2012-13. CALPIA optical enterprises are located at California State Prison, Solano, and the Valley State Prison for Women in Chowchilla (VSPW). VSPW will be known as Valley State Prison as it completes the transition to a men's facility in early 2013.

Partial Deactivation of Modular Bulding Enterprise at Folsom State Prison

The Prison Industry Board approved a partial deactivation of CALPIA's Modular Building Enterprise (MBE) at the November, 2012 board meeting due to the lack of new sales orders for modular buildings over the last 24 months and an absence of new orders. This will result in a corresponding diminishment of the Career Technical Education (CTE) programs hosted at Folsom State Prison as three CTE programs operate within the enterprise at Folsom. Demand for precast concrete furniture will allow the enterprise to remain open in a limited capacity. 66 offender assignments are being eliminated.

The MBE was established to manufacture modular buildings for CDCR and other government entities for medical, program, and administrative space needs. The MBE provided construction skills (carpentry, iron working, and construction labor) for CTE offender participants.

Demand for modular buildings have declined from a high of $25.3 M in FY 2008-09 to no demand in FY 2012-13.

New Modular Building Prototypes

In FY 2012-13, CALPIA invested in several new prototype designs to meet new markets: A telemedicine unit, an incident command unit, and a new low cost, lighter weight modular building. The prototype telemedicine unit was installed at Pelican Bay State Prison in August, 2012 and is providing remote medical services to offenders by way of video conferencing. The remaining two buildings will be completed in the current fiscal year.

Diminishment of the Construction Services and Facilities Maintenance Enterprise

The Prison Industry Board also approved the diminishment of the Construction Services and Facilities Maintenance Enterprise (CSFM) at Folsom State Prison. The Folsom CSFM failed to achieve anticipated revenue in both FY 2010-11 and FY 2011-12. As a result, the CSFM enterprise has not been profitable at the gross level for the last two fiscal years. The CSFM enterprise was established to provide low cost construction and facilities maintenance services to both internal CALPIA customers and external tax-supported customers such as the California Department of Corrections and Rehabilitation (CDCR), California Department of Parks and Recreation and the California Exposition and State Fair (Cal Expo).

The forecasted revenue for CSFM has not materialized, primarily due to a reduction in the California budget that led to fewer construction projects, including a reduction in the demand for CALPIA modular buildings that were installed by CSFM offenders. The CSFM enterprise at the California State Prison-Solano continues to grow and contribute to profitability. This location provides facilities maintenance services for the California Medical Facility and is anticipated to expand to the new Stockton Medical Facility in 2013. Another CSFM location at the California Mens Colony (CMC) will perform lead and asbestos removal at Camp Roberts.

Remanufactured Toner Cartridges

CALPIA launched the Remanufactured Toner Cartridges product line in November, 2010 at Folsom State Prison, offering an easy recycling opportunity to our customers. Initial offerings began with seven different cartridge styles, and in less than one year expanded to 13. Agencies see the fiscal and environmental value of purchasing previously used and remanufactured printer cartridges. In FY 2011-12, Remanufactured Toner Cartridges sales increased 77 percent. In FY 2012-13 sales are expected to increase an additional 35 percent.

AB 900

CALPIA continues to partner with CDCR on projects associated with AB 900 legislation. This partnership includes CALPIA providing metal products required for new correctional facilities. These products such as beds, lockers, and tables, have custom specifications due to the use in correctional settings and CALPIA's production experience and capabilities make CALPIA uniquely qualified to meet CDCR's solution needs.

New Products

AB 900 Projects: Furniture and Metal Products

In support of new re-entry and healthcare facilities associated with AB 900 legislation, CALPIA provided over 1400 items to four facilities in FY 2011-12. Custom correctional products such as beds, desks, lockers, and tables were provided based on the unique specifications of these facilities and the specialized manufacturing experience of CALPIA.

New Furniture Lines (Desks)

New metal study desks were designed to provide educational benefits to offenders while providing security benefits for staff. The first of these are expected to be delivered to the new Stockton Medical Facility in February, 2013. In response to customer requests, CALPIA will also introduce a new table line in FY 2012-13. These tables will have a mobile base and a tabletop that can be rotated vertically for easy and efficient storage and will provide CALPIA customers with the ability to more effectively utilize valuable work space.

In addition, in FY 2011-12 CALPIA streamlined its furniture line, resulting in reduced production costs while still meeting customer needs.

Therapeutic Treatment Modules

The decision in the ***Coleman v. Schwarzenegger*** case resulted in the requirement for CDCR to provide a secure booth for offenders to sit in during mental health care sessions. This metal module allows healthcare professionals to provide, and offenders to receive, care in a secure setting. In support of CDCR to meet the requirements of the court, CALPIA developed a wheelchair accessible module option in FY 2011-12. Hundreds of CALPIA standard and wheelchair accessible therapeutic treatment modules have been provided to CDCR.

Moisture-Wicking Safety Clothing

As a result of an ongoing partnership with Caltrans, CALPIA developed a new American National Standards Institute certified shirt that provides improved health and safety benefits to highway workers operating in a wide range of weather conditions. In FY 2011-12, CALPIA provided over 50,000 shirts to Caltrans highway workers.

Individual Packaged Meals

As a result of a continued partnership with CDCR, CALPIA began providing individual packaged meals for offenders in FY 2011-12, eliminating CDCR staff time and costs associated with individual packaged meal assembly. CALPIA is currently providing over 300,000 individual packaged meals per month to CDCR.

Quality Control and International Organization for Standards (ISO)

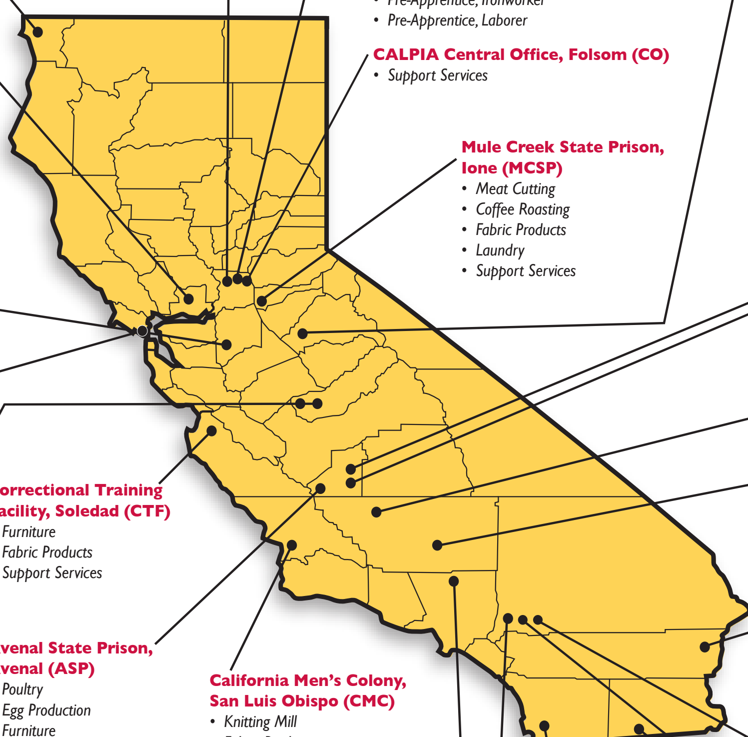
In FY 2011-12 CALPIA expanded the application of International Organization for Standardization (ISO) principles throughout the organization. ISO is the world's largest developer and publisher of International Standards. In preceding years, CALPIA attained ISO certification in its furniture, modular building, and modular furniture factories. In FY 2010-11, CALPIA's wild land fire protective apparel received ISO certification. This ISO certification enabled CALPIA's new line of fire fighting garments to achieve National Firefighter Protection Association (NFPA) certification in September, 2011. The NFPA standard is a national standard for firefighting protective clothing. Implementing and maintaining quality standards affirms CALPIA's commitment to producing superior products while enhancing CALPIA's ability to retain existing customers and attract new customers.

In FY 2011-12, CALPIA reviewed and updated ISO policy and procedure documentation. A re-certification audit conducted in October, 2012 by ABS Quality Evaluations, Inc., verified that CALPIA maintained an effective quality system as documented. In FY 2012-13, CALPIA will be seeking ISO certification for cleaning products, laundry services, dairy and food and beverage packaging enterprises. CALPIA is one of two state correctional industries in the nation that is ISO certified. CALPIA certified 60 offenders as ISO Internal Quality Auditors in FY 2011-12.

PIB Summary of Adopted Action Items 2011-2012

Meeting	Item	Summary 2012
1/13/2011	Item C (11-0113-320-AI)	CALPIA Regulations, Sections 8000, 8007, 8008 Inmate Appeals and Health & Safety Complaint for promulgation through APA.
1/13/2011	Item D (11-0113-321-AI)	Satellite food & beverage packaging Enterprise at CSP-COR; capital investment approx. $800,000; 40 inmate worker assignments anticipated.
1/13/2011	Item E (11-0113-322-AI)	MYR revenues & expenditures $166.8M; Gross profit decrease of $1.8M; $2.3M to fund CTE; utilizing 6,184 inmate positions – reduction of 149 positions (2.4%); funding 598 civil service positions (12.3% salary savings).
1/13/2011	Item F (11-0113-323-AI)	Adoption of $13,014,631 MYR designation of cash to support capital expenditures; $1,065,900 increase.
1/13/2011	Item G1 (11-0113-324-AI)	PIB Report to Legislature FY 2009-10.
4/6/2011	Item B (11-0406-322-AI)	Adoption of Construction Services & Facilities Maintenance Enterprise Statewide; no change to the Revenue Limit of $10M; 20 inmate worker assignments per contact/location.
4/6/2011	Item C (11-0406-323-AI)	Oppose Senate Bill 700 re: allowing CDCR to purchase locally; Reduction by over $4M and up to 60 inmate positions; increase in GF costs to CDCR by $300,000 annually.
4/6/2011	Item D (11-0406-324-AI)	Support Senate Bill 608 re: allowing non-profits to purchase goods & services from CALPIA; possible GF savings $4,900,000 annually.
6/17/2011	Item C (11-0617-299-AP)	Adoption of FY 2011-12 Annual Plan; revenues of $158.7M; increase of 5.2% ($8.65M) from MYR; $6.8M (5.5%) increase of total costs of goods sold; utilizing approximately 5,741 inmate positions, a reduction of 7.2 % from MYR.
6/17/2011	Item D (11-0617-300-AP)	Adoption of $11,303,533 designation of cash to support capital expenditures.
10/21/2011	Item C (11-1021-325-AI)	CALPIA Regulations, Section 8006, Inmate Pay adopted for promulgation through Administrative Procedure Act (APA).
10/21/2011	Item D (11-1021-326-AI)	Support legislation providing net General Fund savings, annual performance-based GF appropriation of approx. $1.15M for CTE program.
10/21/2011	Item E (11-1021-327 AI)	Change & place PIB policy in ISO format re: Transcripts of PIB meetings and public hearings as the official record.
Meeting	**Item**	**Summary 2012**
1/13/2012	Item A (12-0113-328-AI)	Reconsider Individual Prepackaged Meals and hold agenda item over to next PIB meeting after Development and Operations Committee analysis.
1/13/2012	Item B (12-0113-329-AI)	Reconsider AB 109 to amend PC 2933.3 at October, 2012 PIB meeting regarding service credit parity for CALPIA inmates at conservation camp or trained as firefighters (two days of credit for every one day of service).
1/13/2012	Item C (12-0113-330-AI)	Adoption of Year End Audit of Financial Statement FY 2010-11.
1/13/2012	Item D (12-0113-331-AI)	Approval of FY 2011-12 Proposed Mid-Year Revise. Revenues $160.5M, increase 1.5% ($2.3M) from AP estimate; 4.1% (4.8M) increase of total costs of goods sold.
1/13/2012	Item E (12-0113-332-AI)	Approval of $14,937,546 designation of cash to support FY 2011-12 capital expenditures for ongoing operations.
1/13/2012	Item F (12-0113-333-AI)	Approval of PIB Report to the Legislature FY 2010-11.
4/27/2012	Item A (12-0427-334-AI)	Adoption of Regulations, Sections 8000, 8004, 8004.1, 8004.2, 8004.3 & 8004.4 re: Inmate Work/Training & Education for promulgation through APA.
4/27/2012	Item B (12-0427-335-AI)	Oppose Assembly Bill 1507 re: enabling State agencies to enter into purchase contracts for less than $25,000 with CA small, micro or disabled veteran business enterprises; reduction of up to $135M in CALPIA revenues; increase cost to CDCR up to $6.9M.
4/27/2012	Item C (12-0427-336-AI)	Oppose Senate Bill 1162 re: allowing rather than requiring State entities to purchase goods produced by CALPIA; requiring state entities to award contracts to the lowest responsible bidder, reducing Prison Industries Revolving Fund by up to $153M; CDCR incurring GF costs up to $8.1M.
4/27/2012	Item D (12-0427-337-AI)	Approval and concurrence with PIB Development and Operations Committee to proceed with the manufacture of Individual Prepackaged Meals granting a purchase exemption to CDCR for meat-type meals for duration of subsequent contract; have CDCR request DGS establish contract or RFI for meat-type boxed lunches.
6/29/2012	Item A (12-0629-301-AP)	Adoption of FY 2012-13 Annual Plan; revenues of $167.4M; increase of 4.3% ($6.9M) from MYR; $6.8M (5.7%) increase of total costs of goods sold; utilizing approx. 5,408 inmate positions, reduction of 0.2 % from MYR.
6/29/2012	Item B (12-0629-302-AP)	Adoption of $13,285,410 designation of cash to support capital expenditures.
11/16/2012	Item A (12-1116-338-AI)	Approval of the Report to the Prison Industry Board – Career Technical Education (CTE) Programs Fiscal Years 2007-2008 to 2010-2011.
11/16/2012	Item B (12-1116-339-AI)	Approval of partial deactivation of the Modular Building Enterprise at Folsom State Prison.
11/16/2012	Item C (12-1116-340-AI)	Approval of diminishment of the Construction Services & Facilities Maintenance Enterprise at Folsom State Prison.
11/16/2012	Item D (12-1116-341-AI)	Deferred action on diminishment of the Career Technical Education (CTE) programs statewide.
12/18/2012	Item A (12-1218-344-AI)	Approval of Fiscal Year 2011-12 Mid-Year Revise.
12/18/2012	Item B (12-1218-345-AI)	Approval of designation of cash to support FY 2012-13.
12/18/2012	Item C (12-1218-346-AI)	Deferred approval of the Prison Industry Board's Report to the Legislature Fiscal Year 2011-12.
12/18/2012	Item D (12-1218-347-AI)	Adoption of Regulations. CALPIA Personnel Sections 8000-8130 (various).

CALPIA Enterprises by Location



Pelican Bay State Prison, Crescent City (PBSP)
- Laundry

CSP Solano, Vacaville (SOL)
- Metal Products
- Bindery
- Laundry
- Optical
- Support Services
- Construction Services and Facilities Maintenance

Deuel Vocational Institution, Tracy (DVI)
- Dairy
- Support Services

CSP San Quentin, San Quentin (SQ)
- Furniture
- Mattress
- Support Services

Central California Women's Facility, Chowchilla & Valley State Prison for Women, Chowchilla (CCWF/VSPW)
- Crops
- Fabric Products
- Dental Lab
- Optical
- Laundry

On Time Delivery Center, Sacramento (OTD)
- Distribution Center (Northern)

Correctional Training Facility, Soledad (CTF)
- Furniture
- Fabric Products
- Support Services

Avenal State Prison, Avenal (ASP)
- Poultry
- Egg Production
- Furniture
- General Fab/Century
- Laundry
- Support Services

Folsom State Prison, Represa & CSP Sacramento, Represa (FSP)
- Metal Products
- Metal Signs
- License Plates
- Printing
- Laundry
- Modular Building Construction
- Construction Services and Facilities Maintenance
- Digital Services
- Support Services

CTE Programs
- Pre-Apprentice, Carpentry
- Pre-Apprentice, Ironworker
- Pre-Apprentice, Laborer

CALPIA Central Office, Folsom (CO)
- Support Services

Mule Creek State Prison, Ione (MCSP)
- Meat Cutting
- Coffee Roasting
- Fabric Products
- Laundry
- Support Services

California Men's Colony, San Luis Obispo (CMC)
- Knitting Mill
- Fabric Products
- Shoes
- Printing
- Laundry
- Support Services

CSP Los Angeles County, Lancaster (LAC)
- Cleaning Products
- Laundry
- Support Services

Richard J. Donovan, Correctional Facility, San Diego (RJD)
- Bakery
- Shoes
- Laundry
- Support Services

California Institution for Women, Corona (CIW)
- Fabric Products

CTE Program
- Pre-Apprentice, Carpentry

Sierra Conservation Center, Jamestown (SCC)
- Fabric Products

CSP Corcoran & Substance Abuse Treatment Facility, Corcoran (COR)
- Dairy
- Food & Beverage Packaging
- Laundry
- Support Services

On Time Delivery Center, Corcoran (OTD)
- Distribution Center (Central)

Wasco State Prison, Wasco (WAS)
- Laundry

California Correctional Institution, Tehachapi (CCI)
- Fabric Products
- Support Services

Chuckawalla Valley State Prison, Blythe (CVSP)
- Laundry

On Time Delivery Center, Chino (OTD)
- Distribution Center (Southern)

California Institution for Men, Chino (CIM)
- Laundry
- Food & Beverage Packaging
- Support Services

CTE Program
- Marine Technology Training Center

Centinela State Prison, (CEN)
- Fabric Products

*Career Technical Education (CTE) locations appear in blue

Financial Overview with FY 2011-12

Revenues (In Thousands)	FY 10-11 Audited Actual*	FY 11-12 Unaudited Actual	FY 12-13 Approved Annual Plan	FY 12-13 Proposed Mid-Year Revise
Manufacturing	$71,250	$78,038	$73,025	$72,680
Services	63,889	66,342	67,597	65,230
Agricultural	29,259	28,290	26,738	27,216
Total Revenue	**$164,398**	**$172,670**	**$167,360**	**$165,126**

Expenses (In Thousands)				
Cost of Goods Sold				
Manufacturing	$56,896	$65,183	$55,061	$55,253
Services	47,395	49,072	47,709	48,477
Agricultural	25,542	26,468	24,039	24,014
Total Cost of Goods Sold	**$129,833**	**$140,723**	**$126,809**	**$127,744**
Gross Profit	**$34,565**	**$31,947**	**$40,551**	**$37,382**

Selling & Administration (In Thousands)				
Prison Industry Board	$153	$136	$127	$127
Executive Division				
Executive Management	360	273	260	276
Legal	534	590	653	712
External Affairs	139	142	126	136
Operations Division	3,699	3,819	3,290	3,228
Inmate Employability Program (IEP)	675	746	725	697
Marketing Division	3,392	3,497	3,246	3,348
Joint Venture/Free Venture (JV/FV)	354	395	664	664
Administration Division	5,272	4,462	4,284	4,264
Human Resources	886	972	991	977
Staff Development	750	745	687	679
Fiscal Services Bureau	2,386	2,488	2,388	2,641
Career Technical Education Programs (CTE)	1,348	1,265	1,057	1,171
Reimbursements				
CTE	(800)	0	0	0
Joint/Free (JV/FV)	(671)	(652)	(664)	(664)
IEP	(253)	(104)	0	0
Total Central Office	18,224	18,774	17,834	18,256
Distribution/Transportation	11,597	11,887	10,551	11,073
State Pro Rata	3,511	3,798	4,789	4,789
Other Post Employment Benefits	6,270	7,034	6,270	7,034
Furlough Expense	8,619	0	0	0
Total Selling and Administration	**$48,221**	**$41,493**	**$39,444**	**$41,152**
Operating Income/(Loss)	**($13,656)**	**($9,546)**	**$1,107**	**($3,769)**
Non-Operating Revenues/Expenses	**($1,620)**	**$688**	**($344)**	**($344)**
Net Gain/(Loss)	**($15,276)**	**($8,858)**	**$763**	**($4,114)**

* For the purpose of this section, the display of audited financial information was re-configured to remove Pro Rata costs for each category. A State Pro Rata category was added to display associated costs. The Net Gain(Loss) of the fiscal year equals the audited financial statement.

Enterprise Overview

Enterprise	FY 2012-13 Proposed Mid-Year Revise		
	Revenue	Cost of Goods Sold	Gross Profit/ (Loss)
Manufacturing		(In Thousands)	
Furniture	$10,300	$8,632	$1,668
Metal Products	7,700	5,473	2,227
License Plates	12,200	6,099	6,101
General Fabrication (Century Systems)	6,400	6,516	(116)
Bindery	3,050	1, 802	1,248
Knitting Mill	1,332	1,048	284
Fabric Products	20,098	16,278	3,820
Shoes	3,850	3,321	529
Mattresses	2,200	1,721	479
Cleaning Products	5,550	3,650	1,900
Modular Construction	0	713	(713)
Sub-total Manufacturing	$72, 680	$55,253	$17,427
Services			
Meat Cutting	$9,383	$8,111	$1,272
Bakery	3,349	2,202	1,147
Coffee Roasting	1,827	1,510	317
Food & Beverage Packaging	17,768	15,629	2,139
Metal Signs	1,050	819	231
Printing	5,400	2,988	2,412
Dental Lab	700	425	275
Digital Services	400	376	24
Laundry	14,792	10,013	4,779
Optical	10,000	5,356	4,644
Construction Services & Facilities Maintenance	561	1,048	(487)
Sub-total Services	$65,230	$48,477	$16,753
Agricultural			
Dairy/Farm	$13,871	$11,927	$1,944
Crops	1,163	1,224	(61)
Poultry	6,221	5,291	930
Egg Production	5,961	5,572	389
Sub-total Agricultural	$27,216	$24,014	$3,202
Total	**$165,126**	**$127,744**	**$37,382**

Inmate Assignments by Enterprise

Enterprise	FY 10-11 Actuals	FY 11-12 Actuals	FY 12-13 Approved Annual Plan	FY 12-13 Proposed Mid-Year Revise
Manufacturing				
Furniture	476	416	483	483
Metal Products	220	214	239	227
License Plates	102	106	102	105
General Fabrication (Century Systems)	133	133	134	134
Bindery	102	87	105	105
Knitting Mill	95	101	91	91
Fabric Products	1,273	1,245	1,327	1,316
Shoe	170	154	173	173
Mattress	92	61	102	102
Cleaning Products	49	50	50	50
Modular Construction	66	70	66	66
Sub-total Manufacturing	2,778	2,637	2,872	2,852
Services				
Meat Cutting	60	67	68	68
Bakery	66	62	66	66
Coffee Roasting	23	23	25	25
Food & Beverage Packaging	115	158	132	132
Metal Signs	28	32	28	28
Printing	131	138	131	131
Dental Lab	58	56	56	56
Digital Services	13	14	14	18
Laundry	794	750	786	786
Optical	176	185	183	183
Construction Services & Facilities Maintenance	0	29	43	43
Sub-total Services	1,464	1,514	1,532	1,536
Agricultural				
Dairy/Farm	224	227	222	222
Crops	35	31	48	48
Poultry	32	37	81	81
Egg Production	77	60	96	96
Sub-total Agricultural	368	355	447	447
Selling and Administration				
Statewide Administrative Support	292	261	350	357
On-Time Delivery	23	29	25	25
Central Office	27	24	42	42
Career Technical Education Programs	87	50	140	140
Sub-total Selling and Administration	429	364	557	564
Total	**5,039**	**4,870**	**5,408**	**5,399**

Inmate Positions by Location

Location	Average Monthly Filled Inmate Assignments FY 2009-10	FY 2010-11	FY 2011-12
California Institution for Men	241	216	210
California Men's Colony	620	598	593
R. J. Donovan Correctional Facility	282	232	206
Correctional Training Facility	375	381	360
Avenal State Prison	482	424	423
Deuel Vocational Institution	186	151	106
Folsom State Prison/CSP Sacramento/OTD North	540	503	491
San Quentin State Prison	292	236	172
California Institution for Women	178	124	102
California Correctional Institution	270	272	255
California State Prison, Solano - includes CMF	410	390	393
Mule Creek State Prison	350	332	348
Corcoran State Prison/Substance Abuse Treatment Facility	363	334	368
Chuckawalla Valley State Prison	52	38	37
Pelican Bay State Prison	35	19	18
Sierra Conservation Center	125	123	125
Central California Women's Facility/Valley State Prison for Women	406	402	397
California State Prison, Lancaster	91	96	97
Wasco State Prison	86	71	76
Centinela State Prison	69	70	70
Central Office	29	27	23
Total	**5,505**	**5,039**	**4,870**

CALIFORNIA PRISON INDUSTRY AUTHORITY

(A Component Unit of the

State of California)

ANNUAL FINANCIAL REPORT

For the Fiscal Years Ended June 30, 2012 and 2011

MGO Certified Public Accountants.

CALIFORNIA PRISON INDUSTRY AUTHORITY
(A Component Unit of the State of California)

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LA/Century City

Newport Beach

San Diego

Seattle

INDEPENDENT AUDITOR'S REPORT

To the California Prison Industry Authority Board
Folsom, California

We have audited the accompanying balance sheets of California Prison Industry Authority ("CALPIA"), a component unit of the State of California, as of June 30, 2012 and 2011, and the related statements of revenues, expenses and changes in net assets and cash flows for the fiscal years then ended. These financial statements are the responsibility of CALPIA's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of CALPIA's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of CALPIA as of June 30, 2012 and 2011, and the changes in its financial position and its cash flows for the fiscal years then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated December 28, 2012 on our consideration of CALPIA's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grants agreements and other matters for the fiscal year ended June 30, 2012. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

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Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 3 through 14 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Macias Gini & O'Connell LLP

Sacramento, California
December 28, 2012

CALIFORNIA PRISON INDUSTRY AUTHORITY

The following Management Discussion and Analysis (MD&A) applies only to the activities of the California Prison Industry Authority (CALPIA) and should be read in conjunction with its financial statements and related footnotes.

CALPIA is a proprietary component unit of the state of California (State) and is accounted for in the Prison Industries Revolving Fund, which is an internal service fund in the State's basic financial statements. CALPIA does not receive a General Fund appropriation.

Chapter 1549, Statutes of 1982, created CALPIA as a self-supporting state agency. The statutory purposes of the CALPIA are to:

- Develop and operate manufacturing, agricultural, and service enterprises that provide work opportunities for inmates under the jurisdiction of the California Department of Corrections and Rehabilitation ("CDCR");

- Create and maintain working conditions within enterprises, as much like those which prevail in private industry as possible, to assure inmates the opportunity to work productively to earn wages, and to acquire or improve effective work habits or occupational skills;

- Operate a work program for inmates that is self-supporting through the sale of products and services, and reduces the cost of operations of the CDCR.

CALPIA is under the policy direction of an eleven-member board of directors, which reviews and approves the annual budget for the CALPIA. CALPIA manages 57 manufacturing, service, and agricultural factories in 22 institutions. Administrative offices are located in Folsom, California. The goods and services produced by CALPIA's operations are sold principally to departments of the State of California, and other governmental entities. CDCR is CALPIA's largest customer, and accounted for 57% and 62% of all sales in the fiscal years ended June 30, 2012 and 2011, respectively.

Overview of the Financial Statements

The financial statements presented herein include all of the activities of CALPIA as prescribed by statements of the Government Accounting Standards Board (GASB).

The Balance Sheets include all assets and liabilities of CALPIA. They are prepared under the accrual basis of accounting, whereby revenues and receivables are recognized when the service is provided and expenses and liabilities are recognized when incurred, regardless of when cash is exchanged.

The Statements of Revenues, Expenses and Changes in Net Assets present information reflecting how net assets changed during the most recent two fiscal years. All changes in net assets are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of related cash flows. Thus, revenues and expenses are reported in the statement for some items that will result in cash flows in future fiscal periods (e.g., uncollected service charges and earned but unused vacation leave).

The Statements of Cash Flows present information about the cash receipts and cash payments of CALPIA during the two most recent fiscal years. When used with related disclosures and information in the other financial statements, the information provided in these statements should help financial report users assess CALPIA's ability to generate future net cash flows, its ability to meet its obligations as they come due, and its need for external financing. It also provides insight into the reasons for differences between operating income and associated cash receipts and payments, and the effects on CALPIA's financial position of its cash and its noncash investing, capital, and related financing transactions during the year.

Notes to the Basic Financial Statements provide additional information that is essential to a full understanding of the data provided in CALPIA's basic financial statements. The notes are included immediately following the basic financial statements within this report.

Financial Overview

CALPIA has consistently ensured self-sufficiency through the implementation of strategic planning processes and cost containment measures to fulfill its statutory requirement of self-sufficiency. However, after several years of profitability, CALPIA recorded a loss in net assets "decrease" of $8.9 million and $15.3 million during fiscal years 2012 and 2011, respectively, after experiencing a $3.3 million gain "increase" in net assets in fiscal 2010. CALPIA experienced an $8.3 million increase in operating revenues in fiscal 2012 due, in part, to increased revenues from the completion of major projects in its modular office system and modular building enterprises. This revenue gain was negatively impacted by the unanticipated fourth quarter cancellation of CDCR centralized procurement program (CPP) orders totaling $5.5 million. The cancellation was the result of the substantial reduction in inmate population due to the statewide correctional realignment.

Gross profits have been reduced for many CALPIA business lines, in part due to the declining CDCR inmate population. Gross profits were also negatively impacted by an increase in raw material costs, primarily related to CALPIA's food and dairy operations as well as its fabric and knitting mill industries

Additional factors related to the decrease in net assets for fiscal 2012 include a $7.0 million expense for Other Post-Employment Benefits (OPEB) and the loss of $800,000 in CDCR reimbursements for Career Technical Education (CTE) programs. Additionally, the CALPIA assessment for statewide administrative costs increased by $1.0 million in fiscal year 2012, from $3.7 million to $4.7 million.

Notwithstanding the challenges of fiscal 2012, CALPIA remains financially strong. The CALPIA Balance Sheet at June 30, 2012, reflects current assets which are five times greater than current liabilities and almost twice the amount of total liabilities, which are financial indicators that CALPIA is well positioned to meet its short term and long term obligations.

If not for the annual OPEB charge, the loss of fourth quarter CPP sales to CDCR, and the loss of CTE program funding, CALPIA would have been profitable in fiscal 2012.

Correctional Realignment

In October of 2011, the Governor signed AB 109, Committee on Budget, Criminal Justice Alignment, which sought to reduce the inmate population of California prisons with certain identified future offenders being sentenced to incarceration at the local level. The decrease in inmate population caused by the correctional realignment has had a significant impact on the CALPIA revenue for those products and services that are traditionally consumed by the now declining inmate population. CALPIA anticipates that in the 2012-2013 fiscal year revenues will be further reduced by as much as $5.5 million as the impact of the realignment continues to be realized.

Employee Furloughs

Between February 2009 and October 2010, the Governor ordered the vast majority of state workers to take 55 "furlough" days without pay in an effort to reduce the State's General Fund expenditures. Various state employee unions filed suit seeking back pay for furlough days imposed upon them outside of the collective bargaining process. Subsequently, through the collective bargaining process, state employees accepted one unpaid personal leave day (PLP) per month between November 2010 and October 2011, to be used at the employee's discretion.

In fiscal 2011, CALPIA accrued $8.6 million in selling and administrative expense, in anticipation of a court order to compensate its employees for back pay, including interest, for furlough time imposed upon employees.

In January 2012, an agreement was reached between SEIU Local 1000, CASE, and the Governor which settled the civil actions filed by those unions. Pursuant to the terms of the settlement agreement, CALPIA employees would receive reimbursement of all wages withheld during the furlough period, but the employees agreed to waive any right to accrued interest.

The back-pay settlement request was to include all CALPIA civil service employee's including supervisors, managers, confidential and exempt employees, and career executive assignment, but excluded five employees in two bargaining units; BU9 (PECGG) two employees, and BU 10 (CAPS) three employees. These employee unions did not agree to the settlement provisions entered into by SEIU Local 1000 and CASE and did not dismiss their civil action against the Governor. Their civil case remains pending in the Court of Appeals following a judgment entered in the trial court in favor of the employee unions.

In conjunction with the settlement, CALPIA distributed back pay of $7,683,397, recording a gain on settlement of $808,409 and leaving a liability of $126,866 related to the ongoing litigation in the CAPS and PECGG cases.

Postemployment Benefits Other than Pensions

Under Governmental Accounting Standards Board (GASB) Statement No. 45 (GASB 45)—*Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions (OPEB)*, the State is required to recognize the cost of retiree health benefit programs on an accrual basis rather than on a pay as you go basis. The State Controller, who administers GASB 45 accounting requirements for the State, assessed that CALPIA's share of the State's net unfunded OPEB obligation is $7.0 and 6.3 million for the fiscal years 2012 and 2011 respectively. CALPIA recorded these amounts as a "selling and administrative" expense on the operating statement in addition to the actual payments made for OPEB.

The State does not maintain a separate pool of assets to finance future retiree healthcare benefits. As one of the few state agencies required to fund the OPEB obligation from its own proprietary fund, CALPIA actively monitors the costs of retiree health benefits in accordance with Generally Accepted Accounting Principles and the funding policies of the State. As of June 30, 2012, the CALPIA balance sheet reflects a net OPEB obligation of $32.3 million. CALPIA has funded this allocation through cash reserves, and in 2013 will seek authority to reinvest these set aside funds in order to minimize the future obligation through higher interest earnings on the set aside funds.

Factory Closures

In fiscal 2012, CALPIA had no new factory closures. In comparison in fiscal 2011, CALPIA incurred $2.8 million in losses for factories which were closed in fiscal 2011 including $1.3 million of impairment losses at the Deuel Vocational Institution (DVI) furniture factory and lesser amounts at the California Training Facility (CTF) dairy and the Mule Creek State Prison (MCSP) digital services factory.

Strategic Business Plan

CALPIA is financially resilient because management adjusts to the ever-changing business and governmental environment in which it operates. The CALPIA Strategic Business Plan emphasizes the dual priorities of providing inmate rehabilitation and operating a self-sufficient business while enumerating objectives and strategies to accomplish CALPIA's mission. CALPIA new products contributed to the increase in overall CALPIA revenues in 2012 as compared to 2011. Key new product successes in 2012 included wild land fire protection clothing, re-manufactured toner cartridges, highway safety apparel, and new custom metal products. Working in conjunction with the California Department of Forestry and Fire Protection (CAL FIRE), CALPIA developed a new line of wild land fire protection clothing designed to the unique specifications of CAL FIRE. Fiscal 2012 also marked the first full year of production for the re-manufactured toner cartridge product line, resulting in an increase in sales of $129,681 or 74.2% as compared to 2011 and CALPIA customers benefiting from environmentally friendly cartridge solutions. In fiscal 2012, as a result of the ongoing partnership with the Department of Transportation (Caltrans), CALPIA developed clothing that meets the American National Standards Institute (ANSI) requirements and provides safety to thousands of Caltrans employees. CALPIA also continues to partner with CDCR on projects associated with AB900 legislation. This partnership includes CALPIA providing metal products required for new correctional facilities. These products such as beds, lockers, and tables, have custom specifications due to the use in correctional settings and CALPIA's production experience and capabilities make CALPIA uniquely qualified to meet CDCR's solution needs. These efforts are in alignment with Goal 3 of CALPIA's Strategic Business Plan. The objective of Goal 3 is to improve the customer experience, increase customer loyalty, and garner new customers and market share.

Fiscal 2012 was characterized by CALPIA's on-going efforts to adapt to market conditions and improve the overall quality of its products and services. These efforts included expanding the application of International Standards Organization (ISO) principles throughout the organization. In fiscal 2012, CALPIA placed emphasis on existing ISO certifications, by reviewing and updating policy and procedure documentation. A re-certification audit conducted in October 2012 by ABS Quality Evaluations, Inc., verified that CALPIA maintained an effective quality system as documented. In fiscal 2013, CALPIA will be seeking ISO certification for cleaning products, laundry services, dairy, and food and beverage packaging enterprises.

As previously noted above, CALPIA was not created solely to be a business enterprise. CALPIA distinguishes itself as a state program by providing inmates work opportunities and skills they will require to re-enter society as productive citizens. In fiscal 2012, CALPIA employed more than 7000 inmates assigned to 4,870 positions in manufacturing, agricultural and service enterprises. CALPIA invests in curricula for inmates, including 17 programs that offer nationally recognized accredited certifications such as optometry, dental technology, food handling, automotive service, laundry, commercial baking, agriculture, welding and metal stamping. Additionally, through the 2012 fiscal year, CALPIA offered Career Technical Education (CTE) programs in commercial diving, carpentry, and ironworking in partnership with trade unions who offer employment possibilities when inmates are released on parole. CALPIA inmates also earn certificates of proficiency in occupational disciplines which may be utilized upon parole to validate skills and abilities acquired during employment with CALPIA. In fiscal 2012, eleven hundred forty-seven (1,147) CALPIA inmates received a certificate of proficiency, and another two hundred ninety three (293) successfully completed an acredited certification program. CALPIA is currently seeking alternative sources of financing for its CTE programs as the CDCR ceased funding for these programs in fiscal 2011. If no alternative financing sources are found, the CTE programs will be terminated.

In times of economic uncertainty, it is incumbent upon CALPIA to be as responsive as possible to customer demands. In that regard, CALPIA is proud of its contributions to the State. Research indicates that CALPIA saves the State money, both by enhancing the safety of prisons, which helps to reduce staffing costs and by demonstrating lower recidivism rates among those inmates who work in its programs. The recidivism rate of CALPIA inmates is 25% lower than general population inmates and even less for CALPIA inmates participating in CTE programs. Incarceration cost avoidance from CALPIA industries saves the General Fund approximately $8.5 million per year (Bureau of State Audits, May 2011). Further, CALPIA prices are lower than the private sector nearly 60% of the time, which saved CALPIA's five largest customers approximately $3.5 million in fiscal 2010, the latest year for which such information is available. For the remaining products, CALPIA is competitively priced (Bureau of State Audits, May 2011).

In the immediate future, CALPIA must focus on issues which directly affect its ability to operate a business in a corectional environment. Governor Brown signed AB 109 (Chapter 15/2011), which redirects thousands of parolees and new inmates to the jurisdiction of counties, effective October 2011. The effects of this re-alignment reduced CDCR's purchases and have had an impact on the number of inmate employees required to service the enterprises with the reduced revenues, which is expected to continue in fiscal 2013 and 2014.

As our customers benefit from quality goods and services, so do our inmate workers and, ultimately communities throughout California. CALPIA remains optimistic about a future of successful busines enterprises, supported by a dedicated and qualified workforce, working in partnership with satisfied customers that create the best opportunities for the rehabilitation of inmate workers.

Condensed Balance Sheet:

The following table presents the condensed balance sheets for CALPIA as of June 30, 2012, 2011 and 2010:

	2012	2011	2010
Assets			
Cash and cash equivalents	$ 70,838,529	$ 59,682,438	$ 54,884,348
Accounts receviable	8,735,239	7,221,260	10,474,952
Due from state general fund	-	23,400,000	21,000,000
Inventories	41,693,682	42,726,358	43,057,538
Capital assets, net	44,565,093	44,850,226	47,903,931
Other assets	260,103	333,693	293,961
Total assets	166,092,646	$ 178,213,975	$ 177,614,730
Liabilities			
Accounts payable and accrued liabilities	$ 21,278,485	$ 31,365,524	$ 19,566,841
Deferred revenue	1,686,676	2,559,843	4,753,759
Workers'commpensation liability	15,541,448	14,878,827	14,878,827
Net OPEB Obligation	32,258,000	25,224,000	18,954,000
Total liabilities	70,764,609	74,028,194	58,153,427
Net Assets			
Invested in capital assets	44,565,093	44,850,226	47,903,931
Unrestricted net assets	50,762,944	59,335,555	71,557,372
Total net assets	95,328,037	104,185,781	119,461,303
Total liabilities and net assets	$ 166,092,646	$ 178,213,975	$ 177,614,730

Assets

Total assets decreased by $12.1 million at June 30, 2012, compared to June 30, 2011, which is explained by a $23.4 million decrease in due from state general fund, a $1.1 million decrease in inventories, and a $0.3 million decrease in capital assets, which is offset by a $11.2 increase in cash and cash equivalents, and a $1.5 million increase in accounts receivable.

Total assets increased by $0.6 million at June 30, 2011 compared to June 30, 2010, which is explained by a $4.8 million increase in cash and cash equivalents and a $2.4 million increase in due from state general fund, offset by a $3.3 million decrease in accounts receivable, a $3.1 million decrease in capital assets, and a $0.3 million decrease in inventories.

The $11.2 million increase in cash and cash equivalents at June 30, 2012 is explained by the repayment of a $23.4 million short-term loan to the state general fund and $0.3 million investing activities less $6.2 million cash used by operating activities, and $6.3 million for net capital asset acquisitions.

The $1.5 million increase in accounts receivable at June 30, 2012 is mainly attributable to CDCR Department of Juvenile Justice, whose balance is higher than at June 30, 2011 largely due to the purchase of modular buildings to be paid in four annual installments. The decrease in capital assets is attributable to reduced capital outlays and the disposal of older equipment.

The $4.8 million increase in cash and cash equivalents at June 30, 2011 is explained by the positive cash flows from operating activities of $13.1 million and investing activities of $0.2 million, offset by the net outflow of $2.4 million in a short-term loan to the state general fund and $6.1 million for capital asset acquisitions and disposals.

The decrease in inventories at June 30, 2012 is the outcome of utilizing on-hand inventory to satisfy production demands as well as devaluing inventory in the amount of $0.2 million for slow moving and obsolete inventory items. The decrease in capital assets is attributable to the disposal of older equipment throughout CALPIA.

Liabilities

Total liabilities decreased by $3.3 million at June 30, 2012, compared to June 30, 2011. This is explained by a $10.1 million decrease in accounts payable and accrued liabilities offset by a $7.0 million increase in the net liability for OPEB.

Total liabilities increased by $15.9 million at June 30, 2011, compared to June 30, 2010. This is explained by a $11.8 million increase in accounts payable and accrued liabilities and a $6.3 million increase in the net liability for OPEB offset by a decrease in deferred revenue of $2.2 million.

The $10.1 million decrease in accounts payable and accrued liabilities at June 30, 2012 is mostly attributable to the settlement of a lawsuit brought by employee unions contesting employee furloughs, resulting in the $7.8 million issuance of employee back-pay. (See discussion in Overview.) In addition, CALPIA had a $1.6 million decrease in open claims at the end of the fiscal period.

The State annually allocates a portion of retiree health benefit costs to the Prison Industries Revolving Fund. The State recognizes the annual required contribution to the plan which is determined by an actuarial valuation that estimates the present value of future retiree healthcare benefits earned during the employee's working lifetime, including an amortization of the value of unfunded retiree healthcare benefits attributable to employee service earned in prior fiscal years. The State Controller's Office has determined that CALPIA's annual required OPEB contribution is $10.8 million for fiscal 2012. Of this amount, CALPIA contributed $3.8 million; the balance of $7.0 million was accrued as a net OPEB long term liability. CALPIA's annual required OPEB contribution for fiscal 2011 was $9.8 million. Of this amount, CALPIA contributed $3.6 million; the balance of $6.2 million was accrued as a net OPEB long term liability.

The $0.9 million decrease in deferred revenue at June 30, 2012 corresponds to the return of $1.0 million of unused advanced funds to CDCR at the customer's request as well as a balance sheet reclassification of $0.4 million from deferred revenue to customer deposits offset by $0.5 increase in deferred revenues from other customers.

The $2.2 million decrease in deferred revenue at June 30, 2011, corresponds to the revenue recognition of a prior year advance received from CDCR for the construction of modular buildings as well as a balance sheet reclassification of $1.4 million from deferred revenue to customer deposits.

Condensed Statements of Revenues, Expenses and Changes in Net Assets

The following table presents the condensed statements of revenues, expenses and changes in net assets for the years ended June 30, 2012, 2011 and 2010.

	2012	2011	2010
Operating revenues	$ 172,669,580	$ 164,398,239	$ 181,811,217
Cost of goods sold	143,232,093	132,156,694	139,999,941
Gross profit	29,437,487	32,241,545	41,811,276
Selling and administrative expenses	38,983,323	45,896,673	36,849,774
Operating income (loss)	(9,545,836)	(13,655,128)	4,961,502
Non-operating (expenses) revenues, net	688,092	(1,620,394)	(1,680,143)
Increase (decrease) in net assets	(8,857,744)	(15,275,522)	3,281,359
Net assets at beginning of year	104,185,781	119,461,303	116,179,944
Net assets at end of year	$ 95,328,037	$ 104,185,781	$ 119,461,303

Operating Revenues

As presented in the table below, CALPIA sales increased $8.3 million (5.03%) in fiscal 2012 from $164.4 million to $172.7 million, resulting from increases in manufacturing and service enterprises, of $6.8 million (9.53%) and $2.5 million (3.84%), respectively, while sales in the agricultural enterprises decreased by $1.0 million (3.31%). This increase is a marked improvement from fiscal 2011. It is important to note that the increase in revenues did not result in increased gross profit as discussed in the Financial Overview section.

Fiscal 2011 CALPIA sales decreased $17.4 million (9.6%) from $181.8 million to $164.4 million. The drop in revenues is largely attributable to State agencies having fewer discretionary funds to spend .

In manufacturing enterprises, general fabrication (modular office systems) sales increased $7.2 million (112.7%) in fiscal 2012, while the combined sales of furniture, metal products, license plates, fabric products, and modular construction also increased by $3.5 million (7.5%).

Of the $2.5 million increase in sales in service enterprises in fiscal 2012, $2.1 million (14.3%) occurred in food packaging, $0.7 million occurred in optical, and $0.5 million occurred in metal signs. The increase in food packaging revenues are attributable to the introduction of maple syrup packaging, $0.7 million, individual serving packets of peanut butter, $0.9 million, and $0.5 million increased sale of 2-pack cookies. The $0.7 million increase in optical revenue is due to the movement of the Healthy Families Program to Medi-Cal which generated approximately 8,000 additional optical orders each month.

In metal signs the $0.5 million increase in sales is largely due to increased orders from the Department of Parks and Recreation and from DMV and CHP for decals.

The $1.0 million decrease in agricultural sales in fiscal 2012 is explained by a $1.3 million decrease in dairy sales, offset by a $0.4 million increase of poultry sales. Egg production and Crops revenues decreased less than 1% from fiscal 2011.

In manufacturing, the sales of modular buildings increased $1.2 million (135.0%) in fiscal 2012 with the completion of two building projects for CDCR, while the combined sales of the knitting mill, shoe factory, mattress factory, and cleaning products decreased by $2.6 million (-16.5%). The decline in sales in these enterprises partially reflects the cancellation of fourth quarter centralized procurement program (CPP) orders from CDCR due to the redirection of CDCR inmates to counties in accordance with AB 109. The bindery experienced decreased sales revenues of $1.3 million (40.8%) primarily from the decline in sales of handicapped placards to DMV, $1.1 million which increases and declines in alternating 2 year cycles.

	2012	2011	2010
Operating Revenues by Product Line			
Manufaturing:			
Furniture	$ 10,250,388	$ 9,675,374	$ 12,998,752
Metal products	4,177,527	4,085,633	4,844,423
License plates	12,836,502	11,940,815	11,022,264
General fabrication	13,621,163	6,405,117	12,612,758
Bindery	1,887,726	3,186,001	2,066,681
Knitting mill	1,043,224	1,493,281	1,992,224
Fabric products	20,056,748	19,371,098	21,420,228
Silk screening	-	11,200	43,318
Shoe factory	4,362,484	4,847,206	4,819,811
Mattress factory	2,105,064	2,675,061	2,890,369
Cleaning products	5,582,873	6,659,033	7,132,309
Modular construction	2,113,820	899,808	4,564,250
Total manufacturing	78,037,519	71,249,627	86,407,387
Services:			
Meat cutting	9,537,937	9,815,049	9,881,990
Bakery	2,989,955	3,292,298	3,398,686
Coffee roasting	1,863,219	1,927,558	2,100,153
Food packaging	16,617,295	14,544,013	15,129,659
Metal signs	1,450,890	1,000,675	1,133,797
Printing	6,539,715	7,216,236	6,190,498
Dental lab	894,000	696,852	583,790
Digital services	310,975	155,648	33,423
Laundry	15,034,273	14,977,315	15,784,548
Optical	10,965,547	10,263,855	12,394,351
Construction Serv. & Facility Maint.	137,800	-	-
Total services	66,341,606	63,889,499	66,630,895
Agriculture:			
Dairy/farm	14,313,987	15,608,918	14,444,550
Crops	1,184,295	1,193,557	1,428,491
Poultry	6,483,583	6,087,415	6,027,188
Egg production	6,308,590	6,369,223	6,872,706
Total agriculture	28,290,455	29,259,113	28,772,935
Total operating revenues	$ 172,669,580	$ 164,398,239	$ 181,811,217

Cost of Goods Sold

Cost of goods sold increased by $11.1 million (8.4%) in fiscal 2012 from $132.1 million to $143.2 million. The increase in cost of sales corresponds to increased sales throughout various service industries and the general fabrication manufacturing enterprise. Overall, cost of goods sold as a percentage of sales were 83.0% and 80.4% in fiscal years 2012 and 2011 respectively. The increase is primarily due to sales prices of finished goods inventories at fiscal 2011, sold in 2012, that did not reflect the higher costs of raw materials used to produce those finished goods. Gross profit decreased by $2.8 million (8.7%) from $32.2 million to $29.4 million. The decrease in gross profit is primarily comprised a $0.6 million increase in service enterprises, offset by a $1.5 million decrease in manufacturing enterprises, and a $2.0 million decrease in agricultural enterprises. Specifically, in the service enterprises, gross profit increased by $0.6 million in optical, $0.5 million in laundry, $0.5 million in construction services and facilities maintenance, $0.3 million in metal signs, and $0.4 million increase across all other service enterprises. These increases in gross profit for services are offset by $1.0 million decrease in meat cutting, $0.4 million in printing and $0.3 million in coffee roasting, In the manufacturing enterprises, gross profit decreased by $2.5 million in fabric products, $0.8 million in shoes, $0.7 million each in bindery, mattresses, & cleaning products, $0.5 million in knitting, and $0.1 million in metal products, offset by $2.0 million increase in gross profit for furniture, $2.0 increase in general fabrication, $0.4 increase in license plates, and $0.1 increase across all other manufacturing. In the agricultural enterprises, gross profit increased by $0.3 million in crops and $0.2 million in poultry and egg production while the dairy enterprises experienced a decrease in gross profit of $2.5 million. In fiscal year 2011, cost of goods sold decreased by $7.8 million (5.6%) from $140.0 million in 2010 to $132.2 million. This decrease corresponds to reduced sales throughout CALPIA. Overall, cost of goods sold as a percentage of sales were 80.4% and 77.0% in 2011 and 2010, respectively.

This increase is primarily due to a lower level of revenues to cover the fixed cost components of cost of goods sold, increases in certain raw material costs and increased labor costs related to a reduction of the number of employee furlough days, from three per month to one per month.

Selling and Administrative Expenses

Selling and administrative expenses are comprised of distribution and transportation expenses and central office costs. In fiscal 2011, selling and administrative expenses contain a one-time charge of $8.6 million for the anticipated settlement of a lawsuit brought by employee unions contesting employee furloughs (See Overview). In fiscal 2012, the employee furloughs lawsuit was settled and employee back pay issued in June 2012 totaling $7.6 million. Selling and administrative expenses between fiscal years 2012 and 2011 increased by $1.7 million, after giving to the one-time charge of $8.6 million in fiscal 2011. This is explained by the fact that distribution expenses increased $0.5 million due to increased fuel and oil costs and higher sales. Operations Division expenses increased $0.9 million due to absorbing costs associated with Career Technical Education (CTE) programs in absence of reimbursement funding from CDCR in fiscal 2012. Also contributing to the increase of selling and administrative expenses is the unanticipated increase of $0.7 million for OPEB costs. These increases are offset by a $0.8 million decrease in Administration Division largely due to salary savings for vacant positions and elimination of paid overtime. Additionally, the assessment CALPIA receives for statewide administrative costs increased by $1.0 million in fiscal year 2012 from $3.7 million to $4.7 million.

Fiscal year 2011 selling and administrative expenses consist of distribution and transportation charges of $11.6 million, central office costs of $19.4 million, an OPEB charge of $6.3 million, and as previously discussed, a $8.6 million one-time expense to settle a lawsuit brought by employee unions contesting employee furloughs. Overall, selling and administrative expenses increased by $9.1 million (24.6%) in fiscal year 2011 from $36.82 million to $45.9 million. The increase is explained by the $8.6 million furlough expense, while distribution and administrative expenses remained consistent with fiscal 2010 levels of $11.3 million distribution expense and $19.2 million for central office costs.

Non-Operating Revenues (Expenses)

Non-operating revenues (expenses) consist primarily of a loss on disposal of capital assets, interest income (expense) and other expenses. Fiscal 2012 non-operating revenues were $0.7 million as compared to $1.6 total non-operating expenses in fiscal year 2011 due to $1.4 million less in disposal of capital assets and a $0.8 million gain due to the settlement of the furlough litigation.

Product Recall

CALPIA uses an outside consultant to periodically review its product formulations. Subsequent to such a review in July 2012, it was determined that certain fragrance formulations used by CALPIA in its scented bar soap products had been changed by the product supplier and contained an ingredient that has been identified for further study under California's Proposition 65 to determine the maximum level of safe human exposure. As a precautionary measure, CALPIA issued, on July 27, 2012, a product recall to its customers for all bar-soap products sold in fiscal 2012 which was inclusive of on-hand inventories in all customer warehouses. All CALPIA on-hand inventory at June 30, 2012 was also removed from stock and quarantined until its final disposition can be determined. The full impact of expenses incurred due to the recall and replace product to CALPIA customers is not yet known.

Request for Information

The financial report is designed to provide a general overview of CALPIA's finances. For questions concerning any information in this report or for additional financial information, contact Eric Reslock, Chief of External Affairs, at 916-358-1802 or email at Eric.Reslock@calpia.ca.gov.

CALIFORNIA PRISON INDUSTRY AUTHORITY

BALANCE SHEETS

June 30, 2012 and 2011

ASSETS

CURRENT ASSETS	2012	2011
Cash and cash equivalents	$ 57,553,119	$ 48,378,905
Cash designated for capital assets expenditures	13,285,410	11,303,533
Accounts receivable	4,238,731	4,156,041
Related party receivable	4,427,148	3,065,219
Inventories	41,693,682	42,726,358
Due from state general fund	-	23,400,000
Interest receivable	69,360	71,352
Other	260,103	262,341
Total currrent assets	121,527,553	133,363,749
NONCURRENT ASSETS:		
Capital assets not being depreciated	1,233,251	432,889
Capital assets being depreciated, net	43,331,842	44,417,337
TOTAL ASSETS	$ 166,092,646	$ 178,213,975

LIABILITIES AND NET ASSETS

	2012	2011
CURRENT LIABILITIES		
Accounts payable	$ 7,856,498	$ 9,605,261
Accrued expenses and other liabilities	3,509,557	3,734,597
Accrued furlough liability	126,866	8,618,672
Workers' compensation liability-current portion	1,928,647	2,383,232
Deferred revenue	1,686,676	2,559,843
TOTAL CURRENT LIABILITIES	15,108,244	26,901,605
LONG TERM LIABILITIES		
Accrued leave time	9,785,564	9,406,994
Workers' compensation liability	13,612,801	12,495,595
Net OPEB obligation	32,258,000	25,224,000
TOTAL LONG TERM LIABILITIES	55,656,365	47,126,589
TOTAL LIABILITIES	70,764,609	74,028,194
NET ASSETS		
Invested in capital assets	44,565,093	44,850,226
Unrestricted	50,762,944	59,335,555
TOTAL NET ASSETS	95,328,037	104,185,781
TOTAL LIABILITIES AND NET ASSETS	$ 166,092,646	$ 178,213,975

CALIFORNIA PRISON INDUSTRY AUTHORITY

STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS

Years Ended June 30, 2012 and 2011

	2012	2011
OPERATING REVENUES		
Manufacturing	$ 78,037,519	$ 71,249,627
Services	66,341,606	63,889,499
Agriculture	28,290,455	29,259,113
TOTAL OPERATING REVENUES	172,669,580	164,398,239
COST OF GOODS SOLD	143,232,093	132,156,694
GROSS PROFIT	29,437,487	32,241,545
SELLING AND ADMINISTRATIVE EXPENSES	38,983,323	37,278,001
ACCURED FURLOUGH LIABILITY EXPENSES	-	8,618,672
OPERATING LOSS	(9,545,836)	(13,655,128)
NON-OPERATING REVENUES (EXPENSES)		
Interest income	260,845	235,966
Interest expense	(1,277)	(13,933)
Loss from disposal of capital assets	(312,018)	(429,362)
Loss from impairments of capital assets	-	(1,308,501)
Other revenue (expenses)	740,542	(104,564)
TOTAL NON-OPERATING REVENUES (EXPENSES)	688,092	(1,620,394)
Change in net assets	(8,857,744)	(15,275,522)
NET ASSETS - BEGINNING OF YEAR	104,185,781	119,461,303
NET ASSETS - END OF YEAR	$ 95,328,037	$ 104,185,781

See Notes to Basic Financial Statements

CALIFORNIA PRISON INDUSTRY AUTHORITY

STATEMENTS OF CASH FLOWS

Years Ended June 30, 2012 and 2011

	2012	2011
CASH FLOWS FROM OPERATING ACTIVITIES		
Cash receipts from customers	$ 170,351,793	$ 165,458,014
Cash receipts from interfund services provided by other funds of the state	778,658	1,764,899
Cash payments for interfund services used by other funds of the state	(9,291,945)	(9,748,903)
Cash payments to employees for services	(60,691,470)	(53,276,130)
Cash payments to suppliers of goods and services	(107,296,662)	(90,977,446)
Cash payments for other services	(67,867)	(104,564)
Net cash provided by (used in) operating activities	(6,217,494)	13,115,870
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES		
Cash received from (paid to) state general fund	23,400,000	(2,400,000)
Interest expense	(1,278)	(13,933)
Net cash provided by (used in) noncapital financing activities	23,398,722	(2,413,933)
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES		
Acquisitions of capital assets	(6,838,510)	(6,689,225)
Proceeds from sale of capital assets	550,535	552,028
Net cash used in capital and related financing activities	(6,287,975)	(6,137,197)
CASH FLOWS FROM INVESTING ACTIVITIES		
Interest received	262,837	233,350
Net increase in cash and cash equivalents	11,156,091	4,798,090
Cash and cash equivalents at beginning of year	59,682,438	54,884,348
Cash and cash equivalents at end of year	$ 70,838,529	$ 59,682,438

CALIFORNIA PRISON INDUSTRY AUTHORITY

STATEMENTS OF CASH FLOWS (CONTINUED)

Years Ended June 30, 2012 and 2011

	2012	2011
Reconciliation of operating loss to net cash provided by (used in) operating activities:		
Operating loss	$ (9,545,836)	$ (13,655,128)
Adjustments to reconcile operating loss to net cash provided by (used in) operating activities:		
Depreciation	6,261,090	7,453,039
Other expenses	(67,867)	(104,564)
Net effect of changes in:		
Accounts and related party receivables	(1,444,619)	3,253,692
Inventories	1,032,676	331,180
Other assets	2,238	(37,116)
Accounts payable	(1,748,763)	1,113,499
Accrued expenses and other liabilities	(225,040)	2,066,512
Accrued furlough liabilities	(7,683,397)	8,618,672
Workers' compensation liability	662,621	-
Deferred revenue	(873,167)	(2,193,916)
Net OPEB obligation	7,034,000	6,270,000
Net cash provided by (used in) operating activities	$ (6,596,064)	$ 13,115,870

See Notes to Basic Financial Statements

(1) ORGANIZATION

The California Prison Industry Authority ("CALPIA") was established in 1983, as the successor to the California Correctional Industries ("CCI"). It is under the policy direction of an eleven-member board of directors ("Prison Industry Board") and is a component unit of the State of California. CALPIA manages over 57 manufacturing, service, and agriculture factories in 22 institutions that employ inmates at California's penal institutions within the California State Department of Corrections and Rehabilitation ("CDCR"). Administrative offices are located in Folsom, California. The products manufactured by CALPIA's operations are sold principally to departments of the State of California and other governmental entities.

(2) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of accounting - CALPIA uses the accrual basis of accounting. Under this method, revenues and receivables are recorded when earned, and expenses and liabilities are recorded when incurred.

Governmental Accounting Standards Board ("GASB") Statement No. 20 ("GASB No. 20"), *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities That Use Proprietary Fund Accounting*, established standards for accounting and financial reporting for proprietary funds. In accordance with GASB No. 20, CALPIA's proprietary fund accounting and financial reporting practices are based on all applicable GASB pronouncements as well as the following pronouncements issued on, or before November 30, 1989, unless those pronouncements conflict with or contradict GASB pronouncements: Financial Accounting Standards Board ("FASB") Statements and Interpretations, Accounting Principles Board ("APB") Opinions, and Accounting Research Bulletins ("ARB") of the Committee of Accounting Procedures. CALPIA has elected not to apply applicable FASB pronouncements (which are now codified in the Accounting Standards Codification and the Accounting Standards Updates) issued subsequent to November 30, 1989.

Revenue Recognition - Revenues and receivables are recorded when earned, usually upon the shipment of orders, other than modular furniture and building construction. Revenue on modular furniture and building construction is recognized using a method which materially approximates the percentage-of-completion method of accounting, in accordance with Statement of Position ("SOP") 81-1, *Accounting for Performance of Construction-Type and Certain Production-Type Contracts*. Under this method, CALPIA recognizes revenue at the end of each period using output measures in terms of results achieved, to measure the extent of progress toward completion under the contract, on the basis of units of work completed.

Reclassification – Certain prior year amounts have been reclassified to conform with current year financial statement presentation.

Cash and cash equivalents - Cash consists of deposits in the custody of the State of California Treasurer. CALPIA's deposits are subject to the California Government Code and the State Treasurer's Office investment policy for the Pooled Money Investment Account ("PMIA"). Cash not required for current use is invested in the Surplus Money Investment Fund ("SMIF"), while non-SMIF funds are held in operating accounts, all of which are part of the State Treasurer's pooled investment program.

(2) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

These funds are invested through the PMIA and at the direction of the Pooled Money Investment Board, which provides regulatory oversight of such funds. PMIA moneys are limited by State statute to the following investments: U.S. government securities, securities of federally-sponsored agencies, U.S. corporate bonds, interest-bearing time deposits in California banks and savings and loans, prime-rated commercial paper, bankers' acceptances, negotiable certificates of deposits, and other qualifying investments.

The investments in SMIF are reported at amortized cost, which approximates fair value. As of June 30, 2012 and 2011, the weighted average maturity of PMIA investments administered by the State Treasurer's Office was approximately 270 days and 237 days, respectively. Weighted averaged maturity is the average number of days, given a dollar-weighted value of individual investments, that the securities in the portfolio have remaining from the evaluation date to stated maturity. Neither SMIF nor PMIA are rated by credit rating agencies.

Interest earned on cash invested in the SMIF and other pooled funds are prorated to CALPIA based on its average daily balance.

At June 30, 2012, $67,164,000 was invested in SMIF and $3,674,529 was held in operating accounts in the State Treasury pooled investment program. At June 30, 2011 $56,014,000 was invested in SMIF and $3,668,438 was held in operating accounts in the State Treasury pooled investment program. Cash and cash equivalents include cash on hand and temporary cash investments (including SMIF and funds designated for property and equipment acquisitions) with original or remaining maturities of three months or less.

Governmental Accounting Standards Board Statement No. 40, *Deposit and Investment Risk Disclosures – An Amendment of GASB No. 3* ("GASB No. 40") requires that governmental entities provide disclosures regarding deposit and investment credit risk, custodial credit risk, interest rate risk, and concentration of credit risk. CALPIA's deposits in the PMIA are not subject to GASB No. 40 risk disclosures except for the disclosures provided above. Additional information regarding investment risks, including interest rate risk, credit risk and concentration of credit risk of the PMIA can be found in the State's basic financial statements included in its comprehensive annual financial report.

Cash designated for capital asset expenditures - CALPIA segregates its cash which is designated as to use. Designated funds at June 30, 2012 and 2011 represent designations of cash by the Prison Industry Board for certain capital expenditures. The Board designated funds amounting to $13,285,410 and $11,303,533 for certain capital expenditures to be made during the fiscal years ended June 30, 2013 and 2012, respectively.

Concentrations of credit risk - Financial instruments which potentially expose CALPIA to concentrations of credit risk consist primarily of trade accounts receivable.

CALPIA's customer base includes departments of the State of California and other governmental entities. CDCR is the largest customer of CALPIA and accounted for approximately 57% of sales for the fiscal year ended June 30, 2012 and 62% of sales for the fiscal year ended June 30, 2011. As of June 30, 2012 and 2011, CDCR accounted for 51% and 42%, respectively, of total accounts receivable. Management does not believe significant credit risk exists at June 2012 and 2011, as the goods and services produced by CALPIA's operations are sold principally to departments of the State of California and other governmental entities.

(2) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

CALPIA and other state and local agencies' deposits are held in the pooled money account in the custody of the State Treasurer's Office, in which the deposits are insured by federal depository insurance or by collateral held by an agent of the State Treasurer's Office in the State's name.

Accounts receivable - CALPIA has no formal policy regarding the extension of credit and does not use an allowance for doubtful accounts because their customer base is primarily made up of state and local government agencies. As of June 30, 2012 and 2011, CALPIA has receivables of $436,457 and $364,439, respectively, from non-governmental agencies. Historically, CALPIA has not experienced significant losses related to such accounts receivable.

Due from state general fund - During the course of normal operations, the State Controller's Office periodically loans funds from CALPIA's deposits held in the custody of the State Treasurer to the state general fund on a short-term basis for cash management reasons. These transactions are reported as "due from state general fund." As of June 30, 2012 and 2011, due from state general fund totaled $0 and $23,400,000, respectively.

Inventories - Inventories are stated at the lower of cost (as determined using the average cost method) or market. Inventories consist of raw materials, components and subassemblies and finished goods held for sale.

Capital assets - Capital assets are stated at historical cost, net of accumulated depreciation. CALPIA has established a threshold of $5,000 for capitalization of depreciable assets. Expenditures for repairs and maintenance are charged to operations as incurred. Depreciation is computed using the straight-line method over the estimated useful lives of the assets. The estimated useful lives range from 5 to 20 years for equipment, 5 to 30 years for buildings and leasehold improvements, 2 to 3 years for livestock, and 20 years for orchards and 5 years for intangible assets.

Interest expense (net of interest income on unexpended tax-exempt debt proceeds) related to the cost of construction of certain assets is capitalized whenever debt is outstanding and the assets are constructed for use by CALPIA. Capitalized interest is amortized over the related assets' estimated useful lives. CALPIA did not recognize any capitalized interest expense for the fiscal years ended June 30, 2012 and 2011.

In the ordinary course of business, CALPIA opens and closes manufacturing facilities based on economic conditions and industry demand for products. Based on CALPIA's closure policy, management may recommend that the factory remain idle if at a later date it is probable that product demand will increase resulting in the factory being reactivated. If management determines not to reactivate a factory, CALPIA will take one of the following actions: (1) determine if the factory has alternative uses, (2) transfer equipment to operating factories, or (3) pursue other alternatives for disposal. Factories which are closed temporarily are retained in the property accounts as idle facilities and are not depreciated during the temporary closure. At June 30, 2012 the net book value of such factories was not material.

For those facilities which have been closed and will be transferred to CDCR, the related assets are transferred at net book value and a gain or loss is recognized upon the transfer. There were no such transfers during the fiscal years ended June 30, 2012 and 2011.

(2) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Asset impairment - As required by GASB Statement No. 42, management periodically reviews long-lived assets for impairments whenever events or changes in circumstances indicate that the service utility of an asset has declined significantly and unexpectedly.

Impaired capital assets are written down to reduce the related assets to the lower of carrying value or fair value. At June 30, 2012, CALPIA determined that there were no capital assets that are impaired. At June 30, 2011, CALPIA determined that there were capital assets with a net book value of $1,308,501 that were impaired and recorded an impairment charge of $1,308,501 for the fiscal year ended June 30, 2011.

Compensated absences - It is CALPIA's policy to accrue for personal leave time, holiday pay and vacation pay that has been earned but not yet taken by employees. A liability for compensated absences is accrued when incurred and reported in accrued liabilities on the balance sheet. CALPIA employees are not compensated for unused sick leave, but instead are credited with pension service time for unused sick leave. Accordingly, such convertible sick leave is not reflected in the accrued liability for compensated absences. Instead, it is reflected over time in CALPIA's pension contribution.

Deferred revenue - Deferred revenues represent advance payments from customers for the future delivery of products and services.

Net Assets - The difference between assets and liabilities in the balance sheet is labeled as Net Assets and is subdivided into two categories as follows:

> Invested in capital assets - This component of net assets consists of capital assets, net of accumulated depreciation and amortization.
>
> Unrestricted - This component of net assets consists of net assets not restricted for any project or any other purpose.

Operating and non-operating activities - Operating revenues are charges to customers for sales of products and services. Operating expenses consist of cost of sales and selling and administrative expenses. Selling and administrative expenses are comprised of distribution and transportation costs, central office costs, and the annual net unfunded OPEB obligation. All revenues and expenses not meeting these definitions are reported as non-operating revenues and expenses. Distribution and transportation costs include shipping and handling costs related to the delivery of merchandise sold by CALPIA. For the fiscal years ended June 30, 2012 and 2011, such costs were $12,159,338 and $11,596,884, respectively.

Use of estimates in the preparation of financial statements - The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

(2) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

New accounting pronouncements:

In November 2010, the GASB issued Statement No. 61, *The Financial Reporting Entity: Omnibus—an amendment of GASB Statements No. 14 and No. 34*. The objective of this Statement is to improve financial reporting for a governmental financial reporting entity. This Statement modifies certain requirements for inclusion of component units in the financial reporting entity. CALPIA has not determined what impact, if any, this pronouncement will have on the financial statements. The requirements of this Statement are effective for CALPIA's fiscal year ending June 30, 2013.

In December 2010, the GASB issued Statement No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements.* CALPIA has determined that this pronouncement will not have a material impact on the financial statements. The requirements of this Statement are effective for CALPIA's fiscal year ending June 30, 2013.

In June 2010, the GASB issued Statement No. 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position*. GASB Statement No. 63 provides financial reporting guidance for deferred outflows of resources and deferred inflows of resources, introduced and defined in GASB Concepts Statement No. 4. This Statement amends the net asset reporting requirements in Statement No. 34, *Basic Financial Statements—and Management's Discussion and Analysis—for State and Local Governments,* and other pronouncements by incorporating deferred outflows of resources and deferred inflows of resources into the definitions of the required components of the residual measure and by renaming that measure as net position, rather than net assets. CALPIA has determined that this pronouncement will not have a material impact on the financial statements. The requirements of this Statement are effective for CALPIA's fiscal year ending June 30, 2013.

In March 2012, the GASB issued Statement No. 65, *Items Previously Reported as Assets and Liabilities.* This Statement establishes accounting and financial reporting standards that reclassify, as deferred outflows of resources or deferred inflows of resources, certain items that were previously reported as assets and liabilities and recognizes, as outflows of resources or inflows of resources, certain items that were previously reported as assets and liabilities. CALPIA has not determined what impact, if any, this pronouncement will have on the financial statements. The requirements of this Statement are effective for CALPIA's fiscal year ending June 30, 2014.

In March 2012, the GASB issued Statement No. 66, *Technical Corrections-2012-an amendment of GASB Statements No. 10 and No. 62.* The objective of this Statement is to improve accounting and financial reporting for a governmental financial reporting entity by resolving conflicting guidance that resulted from the issuance of two pronouncements, Statements No. 54, Fund Balance Reporting and Governmental Fund Type Definitions, and No. 62, Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements. CALPIA has not determined what impact, if any, this pronouncement will have on the financial statements. The requirements of this Statement are effective for CALPIA's fiscal year ending June 30, 2014.

In June 2012, the GASB issued Statement No. 68, *Accounting and Financial Reporting for Pensions-an amendment of GASB Statement No. 27.* The primary objective of this Statement is to improve accounting and financial reporting by state and local governments for pensions. It also improves information

(2) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

New accounting pronouncements (continued):

provided by state and local governmental employers about financial support for pensions that is provided by other entities. This Statement results from a comprehensive review of the effectiveness of existing standards of accounting and financial reporting for pensions with regard to providing decision-useful information, supporting assessments of accountability and interperiod equity, and creating additional transparency. CALPIA has not determined what impact, if any, this pronouncement will have on the financial statements. The requirements of this Statement are effective for CALPIA's fiscal year ending June 30, 2015.

(3) INVENTORIES

Inventories consist of the following:

	June 30,	
	2012	2011
Raw materials	$23,898,145	$24,744,420
Work-in-process	5,964,847	8,884,590
Finished goods	11,830,690	9,097,348
Total inventories	$41,693,682	$42,726,358

(4) CAPITAL ASSETS

A summary of changes in capital assets during fiscal years 2012 and 2011 is as follows:

	Balance June 30, 2011	Additions & Transfers-in	Deletions & Transfers-out	Balance June 30, 2012
Capital assets, not being depreciated:				
Construction in process	$ 432,889	$ 995,449	$ (195,087)	$ 1,233,251
Total capital assets, not being depreciated	432,889	995,449	(195,087)	1,233,251
Capital assets, being depreciated:				
Equipment	103,538,326	3,861,664	(2,060,088)	105,339,902
Buildings and leasehold improvements, net of transfers	35,895,187	1,171,558	(93,132)	36,973,613
Livestock	4,500,018	1,004,926	(1,192,800)	4,312,144
Orchards	874,716	-	-	874,716
Intangible assets	3,644,018	-	-	3,644,018
Total capital assets, being depreciated	148,452,265	6,038,148	(3,346,020)	151,144,393
Accumulated depreciation and amortization	(104,034,928)	(6,261,090)	2,483,467	(107,812,551)
Total capital assets, being depreciated, net	44,417,337	(222,942)	(862,553)	43,331,842
Capital assets, net	$ 44,850,226	$ 772,507	$ (1,057,640)	$ 44,565,093

(4) CAPITAL ASSETS (CONTINUED)

	Balance June 30, 2010	Additions	Deletions	Balance June 30, 2011
Capital assets, not being depreciated:				
Construction in process	$ 48,128	$ 384,761	$ -	$ 432,889
Total capital assets, not being depreciated	48,128	384,761	-	432,889
Capital assets, being depreciated:				
Equipment	102,737,178	4,293,146	(3,491,998)	103,538,326
Buildings and leasehold improvements, net of transfers	37,518,937	609,387	(2,233,137)	35,895,187
Livestock	5,063,942	1,110,776	(1,674,700)	4,500,018
Orchards	874,716	-	-	874,716
Intangible assets	3,352,863	291,155	-	3,644,018
Total capital assets, being depreciated	149,547,636	6,304,464	(7,399,835)	148,452,265
Accumulated depreciation and amortization	(101,691,833)	(7,453,039)	5,109,944	(104,034,928)
Total capital assets, being depreciated, net	47,855,803	(1,148,575)	(2,289,891)	44,417,337
Capital assets, net	$ 47,903,931	$ (763,814)	$ (2,289,891)	$ 44,850,226

Depreciation expense for the fiscal years ended June 30, 2012 and 2011 was $6,261,090 and $7,453,039, respectively. Depreciation expense includes amortization of intangible assets.

The Prison Industry Board authorized the closure of certain factories because of excess capacity and reduced customer demand for products that were manufactured by such factories. Management has identified certain factory equipment held at the closed factories that will be relocated and placed in service at other factories to replace older equipment currently in service and improve operational efficiency. All other factory equipment and leasehold improvements held at the closed factories, for which management has no plans for continued use, were determined to be impaired capital assets. For the fiscal years ended June 30, 2012 and 2011, the impairment loss recognized on capital assets held at the various closed factories totaled $0 and $1,308,501, respectively. The impairment loss has been reported as a loss from impairments of capital assets in the statements of revenues, expenses and changes in net assets. Management does not consider this event to be unusual in nature or infrequent in occurrence.

(5) ACCRUED EXPENSES AND OTHER LIABILITIES

	June 30,	
	2012	2011
Accrued leave time	$ 486,807	$ 364,090
Customer deposits	387,909	1,416,899
Support charges due to CDCR	1,586,489	987,410
Inmate pay	275,382	332,554
Personal services	235,198	296,749
Sales and use tax	297,620	317,450
Accrued service and expenses	240,152	19,445
Total accrued expenses and other liabilities	$ 3,509,557	$ 3,734,597

(6) ACCRUED FURLOUGH LIABILITY

In February 2009, at the request of the Governor's office, CALPIA and other state agencies instituted involuntary furloughs of substantially all of their employees. Under the arrangement, employees received 3 unpaid furlough days per month. The arrangement ceased in October 2010. Unions representing the furloughed employees sued CALPIA and other state agencies seeking repayment of the lost wages. At June 30, 2011, based on the status of those lawsuits, CALPIA accrued $8.6 million representing its estimate of the wages and interest to be repaid to the involuntarily furloughed employees.

In late January 2012 a settlement agreement was reached in which substantially all CALPIA employees would receive reimbursement of all wages withheld during the furlough period, but would waive any right to accrued interest. Two unions representing five CALPIA employees did not consent to the settlement and their civil case remains pending in the Court of Appeals following a judgment entered in the trial court in their favor. In June 2012 back-pay in the amount of $7,683,397 was distributed to CALPIA employees, excluding the five employees noted above. At June 30, 2012 a reserve of $126,866 remains related to the employees for which a settlement has not been reached. Non-operating income includes $808,409 representing the difference between the original accrual and the sum of the settlement amount and the remaining reserve.

(7) WORKERS' COMPENSATION LIABILITY

CALPIA is exposed to risk of loss related to torts, theft of, damage to, and destruction of assets, injuries to employees, and natural disasters. The State of California self-insures its workers' compensation claims. CALPIA's workers' compensation claims are administered by the State Compensation Insurance Fund as part of the overall State program. CALPIA currently reports claims, expenses and liabilities when it is probable that a loss has occurred and the amount of that loss can be reasonably estimated. These losses include an estimate of claims that have been incurred but not reported and related loss adjustment expenses. Consulting actuaries assist CALPIA in determining its liability for workers' compensation self-insured claims.

The amount of these liabilities was a discounted value of $15,541,448 at June 30, 2012 and $14,878,827 at June 30, 2011. The interest rate used to discount the value of the liabilities for the fiscal years ended June 30, 2012 and 2011, was 3.5%. This liability represents CALPIA's best estimate of its ultimate exposure based on available actuarial information.

Fiscal Year	Beginning of Fiscal Year Liability	Current Year Claims and Changes in Estimates	Claims Payments	Legal and Administrative Expenses Paid	End of Fiscal Year Liability
2011-2012	$14,878,827	$2,591,268	$(1,487,073)	$(441,574)	$15,541,448
2010-2011	$14,878,827	$2,306,992	$(1,910,026)	$(396,966)	$14,878,827

(8) DEFINED BENEFIT PENSION PLAN

Plan description - The State is a member of the California Public Employees' Retirement System ("CalPERS"), an agent multiple-employer pension system, which provides a contributory defined benefit pension for substantially all State employees. CALPIA employees are employees of the State. CALPIA is included in the State Industrial and Safety categories within CalPERS, thereby limiting the availability of certain CALPIA pension data. CalPERS functions as an investment and administrative agent for participating public agencies within the State of California. Departments and agencies within the State of California, including CALPIA, are in a cost-sharing arrangement in which all risks and costs are shared proportionately by participating State agencies.

CalPERS issues a publicly available Comprehensive Annual Financial Report that includes financial statements and required supplementary information for CalPERS. A copy of that report may be obtained by writing CalPERS, Central Supply, P.O. Box 942715, Sacramento, California 94229-2705, or by logging onto the CalPERS web site at www.calpers.ca.gov/.

The pension plan provides retirement benefits, survivor benefits, and death and disability benefits based upon employee's years of credited service, age and final compensation. Vesting occurs after five years of credited service except for second tier benefits, which require 10 years of credited service. Employees who retire at or after 50 with five or more years of service are entitled to a retirement benefit, payable monthly for the remainder of their lives. Several survivors benefit options, which reduce a retiree's unmodified benefit, are available.

(8) DEFINED BENEFIT PENSION PLAN (CONTINUED)

Funding policy - Active members who participate in Social Security under the State Industrial Tier 1 category are required to contribute 8% to 10% of their annual covered salary after excluding the first $513 of gross monthly pay. Active members who do not participate in Social Security under the State Safety and Industrial Tier 1 categories are required to contribute 9% to 12% of their annual covered salary after excluding the first $317 of gross monthly pay. Active members who participate in Social Security under the State Industrial Tier 2 category are not required to make contributions to CalPERS.

CALPIA is required to contribute the actuarially determined remaining amounts necessary to fund the benefits for its members. The actuarial methods and assumptions used are those adopted by the CalPERS Board of Administration. The required employer contribution rate for the fiscal year ended June 30, 2012 was 14.934% and 16.428% for State Industrial and Safety categories, respectively. The required employer contribution rate for the fiscal year ended June 30, 2011 was 18.183% and 20.672% for State Industrial and Safety categories, respectively. The contribution requirements of the plan members are established by State statute and the employer contributions rate is established and may be amended by CalPERS.

Annual pension costs - For the fiscal years ended June 30, 2012, 2011 and 2010, CALPIA's annual pension cost and CALPIA's actual contribution amounted to $4,959,743, $5,322,401, and $5,128,593 respectively. The required contribution for State Industrial and Safety categories for the 2012 and 2011 fiscal years were determined as part of the June 30, 2010 and 2009, actuarial valuations using the entry age normal actuarial cost method with the contributions determined as a percent of pay. The actuarial assumptions included (a) 7.75% investment rate of return (net of administrative expenses), (b) projected salary increases that vary by duration of service ranging from 3.45 to 9.55%, (c) 3.25% overall payroll growth, and (d) 3.0% inflation adjustment.

The actuarial value of CALPIA's assets was determined using a technique that smoothes the effect of short-term volatility in the market value of investments over a 15 year period. The plan's unfunded actuarial accrued liability (or excess assets) is being amortized as a level of percentage of projected payroll on a closed basis. The remaining amortization periods at June 30, 2011 the date of the most recent actuarial valuation, were 12 to 30 years for both the State Industrial Plans and 11 to 30 years for State Safety Plans.

Three-year trend information for State Industrial and Safety Plans:

Fiscal Year Ended June 30,	Annual Pension Cost (APC)	Percentage of APC Contributed	Net Pension Obligation (NPO)
2012	$4,959,743	100%	$ -
2011	$5,322,401	100%	$ -
2010	$5,128,593	100%	$ -

(9) POSTEMPLOYMENT BENEFITS OTHER THAN PENSION

Plan description - CALPIA employees also participate in the State other postemployment benefit ("OPEB") plan. The State OPEB plan is a single-employer defined benefit plan and the Authority participates in the State' plan on a cost-sharing basis. A separate actuarial valuation was not performed for CALPIA. The State's OPEB plan does not issue a separate report.

The State provides medical, prescription drug, and dental benefits to retired statewide employees. The authority for establishing and amending benefits lies with CalPERS and the State Legislature while the authority for establishing and amending the funding policy lies solely with the Legislature.

Funding policy - The State has historically been on a "pay-as-you-go" funding and allocation policy; however, pursuant to the requirements of GASB Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*, ("GASB No. 45") effective for fiscal year 2008, the State amended its allocation methodology to include amortization of its accumulated unfunded postemployment obligations. The State has determined CALPIA's June 30, 2012 and 2011 funding requirements as well as its related 2012 and 2011 contribution credit. The amount allocated to CALPIA at June 30, 2012 and 2011 representing the annual OPEB cost was $10,920,000 and $9,904,000 respectively. Of this amount, $3,886,000 was contributed for 2012 and the balance of $7,034,000 was accrued as a liability. The contribution made for 2011 was $3,634,000 and the balance of $6,270,000 was accrued as a liability.

Annual OPEB cost and Net OPEB obligation - The State of California's annual other postemployment benefit cost is calculated based on the annual required contribution of the employer ("ARC"), an amount actuarially determined by the State in accordance with the parameters of GASB No. 45. The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover normal cost each year and amortize any unfunded actuarial liabilities (or funding excess) over a period not to exceed 30 years. The State determines the allocation for CALPIA based upon the relationship of active employee health benefit costs for CALPIA as compared to the total State active employee health benefit costs. The following table shows the components of CALPIA's allocation of the State's annual OPEB cost for the year, the amount credited to the plan, and changes in the net OPEB obligation as of June 30:

	2012	2011
Annual required contribution	$ 10,794,000	$ 9,809,000
Interest on net OPEB obligation	1,026,000	770,000
Adjustment to annual required contribution	(900,000)	(675,000)
Annual OPEB cost (expense)	10,920,000	9,904,000
Contributions made	(3,886,000)	(3,634,000)
Increase in net OPEB obligation	7,034,000	6,270,000
Net OPEB obligation - beginning of year	25,224,000	18,954,000
Net OPEB obligation - end of year	$ 32,258,000	$ 25,224,000

(9) POSTEMPLOYMENT BENEFITS OTHER THAN PENSION (CONTINUED)

CALPIA's allocation of the annual OPEB cost, the percentage of annual OPEB costs contributed to the plan, and the net OPEB obligation for 2012, 2011 and 2010 were as follows:

Fiscal Year Ended June 30,	Annual OPEB Cost	Percentage of Annual OPEB Cost Contributed	Net OPEB Obligation
2012	$10,920,000	35.6%	$32,258,000
2011	$9,904,000	36.7%	$25,224,000
2010	$9,590,000	34.1%	$18,954,000

Based on information provided to CALPIA by the State, in the June 30, 2011 actuarial valuation, the individual entry age normal cost method was used. A pay-as-you go funding scenario was used by the State. Under the pay-as-you-go funding scenario, the State is assumed to finance retiree healthcare benefits from assets available in the general fund. The State's actuarial assumptions included a 4.5% investment rate of return and an annual healthcare cost trend rate of actual increases for 2012 and of 9.0% in 2013, initially, decreasing each year over the next seven years until the ultimate rate of 4.5% is reached. Both rates included a 3.0% annual inflation assumption. Annual wage inflation is assumed to be 3.25%. The UAAL is being amortized as a level percentage of projected payroll on an open basis over thirty years.

The schedule of funding progress and employer contributions for the State of California for the fiscal year ended June 30, 2012 can be found in the State's basic financial statements included in its comprehensive annual financial report.

(10) RELATED PARTY TRANSACTIONS

Related party transactions with CDCR consisted of the following for the fiscal years ended June 30:

	2012	2011
Assets:		
Accounts receivable	$ 4,427,148	$ 3,065,219
Liabilities:		
Accrued expenses and other liabilities	(1,586,489)	(987,410)
Deferred revenue and customer deposits	(367,551)	(1,396,542)
Revenues:		
Sales	98,955,438	102,376,854
Expenses:		
Support charges paid	(4,741,321)	(4,915,162)

(10) RELATED PARTY TRANSACTIONS (CONTINUED)

The secretary of CDCR is the chairman of the Prison Industry Board. Accounts receivable are for the sale of goods and services delivered to CDCR. Accrued expenses and other liabilities represent expenses incurred for rent and utilities associated with the space owned by CDCR, and used by CALPIA to operate the inmate work programs. Deferred revenue and customer deposits primarily consist of payments received in advance of future delivery of goods and services.

CALPIA has transactions with other agencies of the State in addition to CDCR. For the fiscal years ended June 30, 2012 and 2011 sales to such agencies were $69,719,623 and $57,761,384, respectively. As of June 30, 2012 and 2011, CALPIA had accounts receivable from other state agencies of $3,493,806 and $3,636,744, respectively. Additionally, CALPIA receives an assessment for statewide administrative costs which were $4,788,789 and $3,797,590 for the fiscal years ended June 30, 2012 and 2011 respectively.

(11) CONTINGENCIES

CALPIA uses an outside consultant to periodically review its product formulations. In July 2012, in conjunction with such a review, it was determined that certain varieties of scented bar soap that it produced contained a potential carcinogen as a result of a change in the supplier's fragrance formulations. CALPIA voluntarily recalled the bar soap that it had produced using the fragrance, including product that had been produced and sold prior to June 30, 2012. CALPIA is evaluating its options for disposing of the recalled product, including reselling the product with full disclosure of the potential carcinogen to customers outside the state or scrapping the product. CALPIA has estimated the potential loss associated with the recall, including transportation and distribution costs, to range from approximately $300,000 to $1 million. CALPIA may be subject to lawsuits related to this matter, but does not believe that the amount if any that it would be obligated to pay would be significant.

CALPIA is involved in various legal actions arising in the ordinary course of business. In the opinion of management, after consulting with legal counsel, CALPIA intends to defend these other cases vigorously and believes that the ultimate liability, if any, will not be material to the financial position of CALPIA.

(12) COMMITMENTS

Warranties - CALPIA provides a warranty on its office and miscellaneous furniture and bedding products for a period of five years. CALPIA has not established a reserve for warranty expense. The affect on operations are deemed by management to be immaterial. Such costs are expensed when incurred.

Rental payments - Future minimum rental payments required under operating leases that have initial or remaining noncancellable lease terms in excess of one year expiring in January 2020 as of June 30, 2012, are as follows:

(12) COMMITMENTS (CONTINUED)

Fiscal Year Ended June 30,	Rent Payments
2013	$ 393,864
2014	386,232
2015	378,600
2016	377,328
2017	384,960
2018	392,592
2019	400,229
2020	236,068
Total	$ 2,949,873

Total rental expense for all operating leases was $506,769 and $570,096 for the fiscal years ended June 30, 2012 and 2011, respectively.

SUPPLEMENTAL INFORMATION

MGO Certified Public Accountants.

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Oakland

LA/Century City

Newport Beach

San Diego

Seattle

INDEPENDENT AUDITOR'S REPORT ON SUPPLEMENTAL INFORMATION

To the California Prison Industry Authority Board
Folsom, California

We have audited the basic financial statements of California Prison Industry Authority ("CALPIA") as of and for the fiscal years ended June 30, 2012 and 2011, and have issued our report thereon dated December 28, 2012. Our audit was conducted for the purpose of forming an opinion on the financial statements as a whole. The supplemental Balance Sheet, Statements of Revenues, Expenses and Changes in Net Assets, and Statements of Cash Flows as of and for the fiscal years ended June 30, 2012 and 2011, classified in accordance with the State Controller's Office Instructions (collectively the "SCO financial statements") are presented for purposes of additional analysis and are not a required part of the financial statements. The SCO financial statements are the responsibility of management and were derived from and relate directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records use to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the financial statements as a whole.

Macias Gini & O'Connell LLP

Sacramento, California
December 28, 2012

CALIFORNIA PRISON INDUSTRY AUTHORITY
INTERNAL SERVICE FUND

BALANCE SHEETS
CLASSIFIED IN ACCORDANCE WITH THE STATE CONTROLLER'S INSTRUCTIONS

June 30, 2012 and 2011
(in thousands)

ASSETS

	2012	2011
CURRENT ASSETS		
Cash and pooled investments	$ 70,839	$ 59,683
Receivables, (net)	744	1,003
Due from other funds	7,760	29,628
Due from other governments	231	61
Prepaid items	260	262
Inventories, at cost	41,694	42,726
TOTAL CURRENT ASSETS	121,528	133,363
NONCURRENT ASSETS		
Nondepreciable capital assets:		
Construction in process	1,233	433
Depreciable capital assets:		
Buildings	5,288	5,288
Leasehold improvements	31,686	30,607
Equipment	105,340	103,538
Livestock	4,312	4,500
Orchards	875	875
Intangible assets	3,644	3,644
TOTAL CAPITAL ASSETS	152,378	148,885
Accumulated depreciation:		
Buildings	(3,322)	(3,097)
Leasehold improvements	(23,458)	(22,402)
Equipment	(76,503)	(74,005)
Livestock	(447)	(576)
Orchards	(711)	(670)
Intangible assets	(3,372)	(3,285)
TOTAL ACCUMULATED DEPRECIATION	(107,813)	(104,035)
TOTAL NONCURRENT ASSETS	44,565	44,850
TOTAL ASSETS	$ 166,093	$ 178,213

LIABILITIES AND NET ASSETS

	2012	2011
CURRENT LIABILITIES		
Accounts payable and other	$ 7,856	$ 9,605
Due to other funds	2,416	1,949
Deferred revenue	1,687	2,560
Compensated absences payable	10,273	9,771
Other current liabilities	2,662	12,423
TOTAL CURRENT LIABILITIES	24,894	36,308
NONCURRENT LIABILITIES		
Net OPEB obligation	32,258	25,224
Other non-current liabilities	13,613	12,496
TOTAL NONCURRENT LIABILITIES	45,871	37,720
TOTAL LIABILITIES	70,765	74,028
NET ASSETS		
Invested in capital assets	44,565	44,850
Unrestricted net assets	50,763	59,335
TOTAL NET ASSETS	95,328	104,185
TOTAL LIABILITIES AND NET ASSETS	$ 166,093	$ 178,213

CALIFORNIA PRISON INDUSTRY AUTHORITY
INTERNAL SERVICE FUND

STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS CLASSIFIED IN ACCORDANCE WITH THE STATE CONTROLLER'S INSTRUCTIONS

Years Ended June 30, 2012 and 2011
(in thousands)

OPERATING REVENUES	2012	2011
Services and sales	$ 172,670	$ 164,398
OPERATING EXPENSES		
Personal services	(61,084)	(68,908)
Supplies	(2,211)	(2,124)
Services and charges	(112,659)	(99,568)
Depreciation	(6,261)	(7,453)
Total operating expenses	(182,215)	(178,053)
OPERATING INCOME (LOSS)	(9,545)	(13,655)
NONOPERATING REVENUES (EXPENSES)		
Interest income	261	235
Interest expense	(1)	(14)
Loss on disposal and impairment of of capital assets	(312)	(1,738)
Other expense	740	(104)
Total nonoperating (expenses) revenues	688	(1,621)
Change in net assets	(8,857)	(15,276)
NET ASSETS AT BEGINNING OF YEAR	104,185	119,461
NET ASSETS AT END OF YEAR	$ 95,328	$ 104,185

CALIFORNIA PRISON INDUSTRY AUTHORITY
INTERNAL SERVICE FUND

STATEMENTS OF CASH FLOWS
CLASSIFIED IN ACCORDANCE WITH THE STATE
CONTROLLER'S INSTRUCTIONS

Years Ended June 30, 2012 and 2011
(in thousands)

	2012	2011
CASH FLOWS FROM OPERATING ACTIVITIES		
Receipts from customers	$ 170,352	$ 165,458
Receipts from interfund services provided	779	1,765
Payments for interfund services used	(9,292)	(9,749)
Payments to employees	(60,692)	(53,276)
Payments to suppliers	(107,297)	(90,978)
Payments for other services	(68)	(104)
Net cash provided by (used in) operating activities	(6,218)	13,116
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES		
Change in interfund receivable	23,400	(2,399)
Interest expense	(1)	(14)
Net cash provided by (used in) noncapital financing activities	23,399	(2,413)
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES		
Acquisitions of capital assets	(6,839)	(6,689)
Proceeds from sale of capital assets	551	552
Net cash used in capital and related financing activities	(6,288)	(6,137)
CASH FLOWS FROM INVESTING ACTIVITIES		
Interest on investments	263	233
Net increase (decrease) in cash and pooled investments	11,156	4,799
Cash and pooled investments, beginning of year	59,683	54,884
Cash and pooled investments, end of year	$ 70,839	$ 59,683

CALIFORNIA PRISON INDUSTRY AUTHORITY
INTERNAL SERVICE FUND

STATEMENTS OF CASH FLOWS
CLASSIFIED IN ACCORDANCE WITH THE STATE
CONTROLLER'S INSTRUCTIONS

Years Ended June 30, 2012 and 2011
(in thousands)

RECONCILIATION OF OPERATING LOSS TO NET CASH PROVIDED BY (USED IN) OPERATING ACTIVITIES	**2012**	**2011**
Operating loss	$ (9,545)	$ (13,655)
Adjustments to reconcile operating loss to net cash provided by (used in) operating activities:		
Depreciation	6,261	7,453
Other fees	740	(104)
Net effect of changes in:		
Receivables	259	(34)
Due from other funds	(1,534)	2,949
Due from other governments	(170)	339
Prepaid items	2	(37)
Inventories	1,032	331
Accounts payable and other	(1,749)	1,113
Due to other funds	467	(116)
Deferred revenue	(873)	(2,194)
Other current liabilities	(9,761)	10,035
Compensated absenses payable	502	766
Other liabilities	8,151	6,270
Total adjustments	3,327	26,771
Net cash provided by (used in) operating activities	$ (6,218)	$ 13,116

20%